THE AUSTRALIAN NATIONAL UNIVERSITY

DEGREE OF MASTER OF ECONOMICS

At a Meeting of the Standing Committee of the Council of the Australian National University held on the 11th October, 1963,

Paul Douglas ABBOTT

was admitted to the degree of

MASTER OF ECONOMICS
EUROPEAN ECONOMIC INTEGRATION
AND ITS EFFECTS ON AUSTRALIA.

Thesis submitted for
degree of Master of Economics,
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Paul Douglas Abbott
Preface to thesis on
European Economic Integration and its
effects on Australia

This thesis was started at a time when British negotiations for a free trade area had broken down and it was not at all clear that Britain was likely to go into Europe.

When the thesis was substantially finished it became likely that Britain would make an early move into the Community and it was therefore considered advisable to delay completion until this move had been accomplished and the nature of the safeguards for Australian trade were known.

Although this move has still not been made, published reports make it apparent that the Six regard any maintenance of preferences or arrangements of a preferential nature between Britain and Australia as being contrary to the Rome Treaty. In these circumstances it is apparent that no special safeguards for Australian trade can be anticipated. Although there has been some suggestion that global commodity agreements will be worked out, it is apparent that it will not be for a considerable time that the terms of any such agreement will be finalised and even then their precise benefit to Australia will have to be determined in practice.
It is therefore considered that it would not be appropriate to delay the presentation of this thesis further and that it can advantageously be submitted as an appraisal of the situation as it appears in November 1962.

Although a short note appears in the historical chapter on economic integration in eastern Europe, no attempt has been made to embrace this rather distinct subject in the body of the thesis.

The historical chapter has turned out to be rather lengthy and detailed in relation to the rest of the thesis but has been retained in its current form because of its usefulness as a document of reference.

P.D. Abbott.

November 1962.
Glossary of main abbreviations.

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<th>Description</th>
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<tr>
<td>COMECON.</td>
<td>Council for Mutual Economic Cooperation.</td>
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<td>E.C.S.C.</td>
<td>European Coal and Steel Community.</td>
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<td>E.E.C.</td>
<td>European Economic Community.</td>
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<td>E.F.T.A.</td>
<td>European Free Trade Association.</td>
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<td>Euratom.</td>
<td>European Atomic Energy Community.</td>
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<td>G.A.T.T.</td>
<td>General Agreement on Tariffs and Trade.</td>
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<td>Rome Treaty.</td>
<td>Treaty establishing the European Economic Community.</td>
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<td>Schuman Plan.</td>
<td>Proposal to create E.C.S.C.</td>
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<tr>
<td>Seven.</td>
<td>Austria, Britain, Denmark, Norway, Portugal, Sweden and Switzerland.</td>
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<tr>
<td>Six.</td>
<td>Belgium, France, German Federal Republic, Italy, Luxemburg, Netherlands.</td>
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I. HISTORY OF EUROPEAN ECONOMIC INTEGRATION.
Chapter 1.

The modern concept of regional economic integration derives from the principle of the customs union which was developed in the nineteenth century. This has been defined as "any agreement or union of separate states undertaken with a view to eliminating or reducing tariffs between them while maintaining tariff barriers against the outside world." (1)

(a) The Zollverein.

The most important customs union of the nineteenth century was the Zollverein which was gradually developed by Prussia throughout that century. The new Prussian tariff of 1818, whose object was mainly to protect new industries, created in the first place difficulties for small independent enclaves. Schwarzburg-Sondershausen joined the Prussian customs system in 1819 in order to obtain a share of the customs revenue which goods entering its territory from outside Prussia had to pay when they passed over the Prussian border whilst the accession of the Anhalt duchies in 1828 was due to the vigorous measures taken by the Prussians against smuggling from the territory into Prussia of goods that had been imported via the Elbe river. (2) The first state to adhere to the Prussian system that was not surrounded by Prussian territory and which consequently continued to maintain its own customs posts even after joining the system was Hesse-Darmstadt.
Its accession in 1828 was due to financial difficulties and to the burden of protecting a long frontier. In many ways this accession formed a model for later accessions. When this was first mooted Prussia was not at all anxious to secure this accession which was economically burdensome to her but von Motz, the Prussian finance minister, realised the importance of progressively linking the eastern and western territories of the kingdom. (3)

In the meantime, there had been negotiations between other German states for the formation of a customs union. These came to nothing because of the protectionist policies of the south German states which were opposed to the free trade policies of the Rhenish states. (4) In 1827 an increased tariff, that of Bavaria, had once again the effect of promoting a customs union, in this case between itself and a smaller neighbour, Wurttemberg. This was known as the South German customs union. At the end of 1828, a considerable number of the remaining states formed what was known as the Middle German customs union; this was a loose arrangement without a common tariff, dedicated to keeping open trade routes in central Germany and politically supported by Austria and England. (5)

(1) Encyclopaedia Britannica, 1958, Customs Unions. Although the encyclopaedia refers to this definition as a strict one, it is in fact much looser than that in Article XXIV of the General Agreement on Tariffs and Trade 1947/48. (2) W.O. Henderson, The Zollverein, pages 44 to 47. (3) W.O. Henderson, op.cit., pages 50 to 54. (4) W.O. Henderson, op.cit., page 59. (5) W.O. Henderson, op.cit., page 65. We now call such a union without a common tariff, a "Free Trade Area".
In 1829 the South German union made overtures to Prussia, occasioned largely by dislike of the former for the Middle German union. A preferential agreement was in that year concluded between the North and South German unions. (6) Motz managed to persuade some of the Thuringian duchies to permit the building of a road between the two unions and he also induced Holland to relax navigation restrictions on the Rhine which had impeded transport affecting the two unions.

Motz died in 1830 but his work sealed the fate of the Middle German union. (7) Following the secession of Saxony from the Middle German union the Zollverein was formed in 1833 and commenced operation at the beginning of the following year. It was now only a matter of time before the rest of the central German states were to accede.

A more serious rival to German unification was the Steuerverein, or Tax Union, formed from 1834 to 1838 in the north west between Hanover, Brunswick, Oldenburg and Lippe-Schaumburg. However, Brunswick quarrelled with Hanover in 1841 and joined the Zollverein. (8) Hanover opened negotiation with the Zollverein in 1842 but demanded a number of concessions and it was not in fact until 1851 that the union was consummated, followed shortly afterwards by the accession of the remaining two members of the Tax Union. (9)

Luxemburg joined the Zollverein in 1842, the Mecklenburgs and Lubeck in 1868, Hamburg in 1881 and Bremen in 1884.

From the 1830's Prussia increasingly realised the political importance of the Zollverein and rebutted frequent attempts by Austria either to join the Zollverein or to win away the south German states to a rival union. (10) Prussia sought on several occasions to reduce the common tariff of the Zollverein to make it more difficult for protectionist Austria to join. An important test came with a Franco-Prussian treaty of 1862 which not only obliged the Zollverein to abolish preferential customs treatment accorded to Austria by a treaty of 1853 but also required considerable reductions of the common tariff. Despite opposition by Bavaria, Wurttemberg and Hanover these reductions were implemented. (11)

Following the defeat of Austria by Prussia in the seven weeks' war of 1866, the Austrian connection with the German confederation was severed. Prussia annexed a number of north German states including Schleswig and Holstein which Prussia and Austria had wrested from Denmark two years earlier and formed a North German confederation.

(10) For example in 1858/2, 1857 and 1862. (11) W.O. Henderson, op.cit., page 286.
Following the defeat of France in 1870 the south German states joined the confederation to form the German Empire. German economic integration thenceforth became of historical importance only.

The developments in nineteenth century Germany have tended to provoke the generalisation that political unity necessarily follows economic integration. This is the opposite of what actually happened in Italy where "trade followed the flag". Moreover there still exist in Europe today customs unions between small states and more powerful neighbours that have not led to integration. These include the customs union dating from 1862 between San Marino and Italy and that of 1865 of Monaco with France. Two nineteenth century unions, that of Luxemburg with the Zollverein and of Liechtenstein with Austria, passed in the 1920's to new associations with Belgium and Switzerland respectively.

(b) Obstacles to further integration.

Objections by third countries with treaty rights have caused the abandonment of several customs union proposals in Europe. A customs union treaty of 1857 between Austria and Modena was abandoned on the objections of Sardinia and the Zollverein.
Austria had guaranteed Sardinia most-favoured-nation tariff treatment. There was an exception in the treaty in favour of any complete customs union entered into by Austria. It was objected that the customs union with Modena would be incomplete. A customs union between Bulgaria and Serbia created by treaty of 1904 was also dropped on objection by Austria-Hungary, assured by treaty with Serbia of most-favoured-nation tariff treatment; in this case completeness of the union was irrelevant as there was no exception in the treaty. On the other hand the proposed anschluss of Austria with Germany of 1931 was abandoned mainly because of its inconsistency with Austria's obligations under the treaty of St. Germain to maintain its political independence. (12)

Proposals for European customs unions go back to the 1880's. The early proposals were openly directed against the United States which had most-favoured-nation treaties with European countries who were reducing their tariffs by mutual bargaining whilst the United States tariff was rising. (13)

(12) These three cases are discussed at length by Jacob Viner, The Customs Union Issues, 1950 pages 7 to 12. (13) Jacob Viner, op. cit., page 22.
In 1897 Count Goluchowski, Austrian foreign minister, in a circular letter to other European countries, proposed that the countries of Europe combine to take concerted action directed against American commercial competition. (14)

At an Allied Economic Conference held at Paris in June 1916 France, Italy and Britain agreed to take concerted action during and after the war in the field of commercial policy. This aroused opposition in the United States as the move was interpreted as an intention not only to discriminate against the Central Powers but also against other countries. Subsequent American participation in the war led to the abandonment of the proposals. (15)

At the World Economic Conference held under League of Nations auspices at Geneva in 1927 a representative of the Austrian Committee of the International Chamber of Commerce proposed "joint and parallel negotiations conducted between as large a group as possible of European states for the purpose of substantially lowering their customs tariffs." The resolutions of the conference do not, however, indicate that the suggestion was adopted although there is some mention of mutual agreements between states as being a desirable matter for study by the League of Nations. (16)

Throughout the inter-war period the movement towards plurilateral agreements encountered an over-riding obstacle in the most-favoured-nation clause of bilateral agreements. Although in 1929 the Economic Committee of the League of Nations gave a qualified approval to plurilateral agreements of a "general character" and recommended the insertion of qualifications to the most-favoured-nation clause in commercial treaties to permit such agreements to be implemented, the process of revision of treaties was too slow to be effective as one unrevised treaty could block the operation of a plurilateral agreement. (17) Thus the Ouchy Convention of 1932, which provided for the preferential reduction of tariffs between what are now known as the Benelux countries, never came into force as Britain and the United States refused to waive their most-favoured-nation rights to permit implementation. The Ottawa Conference, 1932, passed a resolution declaring that regional agreements should not be allowed to override most-favoured-nation obligations. This seems surprising in view of the extension of Imperial Preference by the Conference.

An attempt on a fresh basis was made by the Hague Convention of 1937, concluded between Scandinavian countries and the present members of Benelux. Under this convention preferential relaxations of quantitative restrictions between the parties were to be effected.

The Netherlands declined to renew the convention after the first year, one of the grounds of its refusal being that Britain had contended to her that the most-favoured-nation clause applied to quantitative restrictions as well as to tariffs. (18) The 1933 Monetary and Economic Conference held at London in fact made no progress on this issue but it is noteworthy for a proposal by Mr. Cordell Hull, the United States Secretary of State, that plurilateral agreements conforming with certain rather comprehensive criteria should be considered as consistent with the most-favoured-nation clause. (19)

(c) The easing of obstacles.

It is perhaps this change of heart on the part of the United States which has made economic integration such an important and live issue in Europe following the second world war. As a result of Point Four of the Atlantic Charter declaration of August, 1941, which provided that the United States and Britain would endeavour, with due respect for their existing obligations, to further enjoyment by all states, great or small, victor or vanquished, of access, on equal terms to the trade and to the raw materials of the world which were needed for their economic prosperity, the United States formulated "Proposals for the Expansion of World Trade and Employment".

(19) Jacob Viner, op.cit., pages 32 to 36.
These were discussed with Britain at the Anglo-American Financial and Economic Discussions held at Washington from September to December, 1945. No-one reading the text of Point Four would imagine that it was to result in a considerable weakening of the most-favoured-nation clause, as has in fact been the case. The United States proposals, after setting out the general principles of commercial policy, state in paragraph 2 of Section H "the provisions of Chapter III should not prevent any member from joining a customs union, provided that such customs union meets certain agreed criteria." These criteria were spelled out in the Suggested Draft Charter for an International Trade Organisation of July 1946 and were incorporated in the General Agreement on Tariffs and Trade of 1947; the relevant provision being revised at Havana in 1948. The adherence of the majority of trading nations to the G.A.T.T. has had the effect of modifying the rigidity of the most-favoured-nation clause contained in bilateral agreements and has in fact removed the obstacles to the formation of customs unions. This obstacle may still exist where countries, not members of G.A.T.T., are entitled to most-favoured-nation treatment under bilateral agreements not containing exceptions in respect of customs unions. Equally important is the transfer of jurisdiction as to what is or what is not a permissible form of customs union from international tribunals to the flexible forum of the G.A.T.T. The G.A.T.T. is, generally speaking, unable to enforce strict compliance with its rules and in addition has an unlimited power
to grant waivers therefrom. As a result it not possible today to say that there is any definable limit on the type of regional economic association that may be formed. Rules and in fact quite detailed rules exist but it is a political question how far compliance with them is obligatory.

The integration impetus consequent on the Second World War

From 1944 onwards movements for economic integration in western Europe can be divided into first a global movement deriving largely from the Paris Economic Conference of July 1947 and three localised movements, Benelux, the Franco-Italian scheme which appears to have inspired the European Economic Community and proposals for economic union in Scandinavia. Later there was a split of the global movement into two sectors, one attracted to the Community and the other to Britain but the members of the latter group are now being attracted to the Community.

(d) Benelux

The first step towards achieving close economic cooperation between the Belgo-Luxemburg Economic Union and the Netherlands was taken on September 6, 1944 when the governments of the three countries in exile signed a treaty establishing Benelux. This provided, after the liberation of the countries, for the mutual abolition of import duties and the establishment of a common customs tariff via-a-vis third countries. On 1 January, 1948 the London agreement, with some amendments due to changed conditions, was put into operation. Legislation had already been passed by the Parliaments of the three countries in April and
May 1947 to establish the common tariff. This tariff had been worked out following a decision by the three governments in April 1946 to go ahead with its preparation.

At a ministerial conference in Luxemburg in October, 1949 the three countries concluded the so-called Pre-Union Treaty as an introductory stage to full economic union. The main step forward in this treaty was the provision for progressive removal of quantitative restrictions except for special arrangements on some agricultural products. Further steps forward were taken in 1958 when an agreement was reached for elimination of the agricultural import restrictions over a period of five years and an Inter-parliamentary Benelux Advisory Council was established. On 3 February, 1958 the Benelux Economic Union Treaty was signed. It came into force on 1 November 1960. Despite difficulties in the agricultural sector and in regard to excise duties which have hindered completion of the union, Benelux has been internationally accepted as a customs union since 1947.

(e) Scandinavia

In February 1948 a Joint Committee for Scandinavian Economic Cooperation was set up to study the possibilities of a customs union between Denmark, Norway, Sweden and Iceland. The Committee in January 1950 reported that there was at present no basis for realising such a customs union, in particular because of the effect it would have on Norwegian industry.
Later, in January, 1950, the Governments of Britain, Denmark, Norway and Sweden set up an Anglo-Scandinavian Economic Committee, known as UNISCAN. The main object of the committee, which is still in operation, is to continue close cooperation in the financial sphere and to accelerate relaxation of mutual payments restrictions.

Further movements for economic cooperation in Scandinavia have concerned Denmark, Norway, Sweden and Finland and derive from the Nordic Council, a consultative body consisting of representatives of the parliaments of the four countries. In July, 1954 a single labour market for the four countries was established and in the following month the Council adopted a recommendation of its economic committee that the possibilities of establishing a common market should be investigated. (20) Ministers of the four countries met at the end of October, 1954 and decided to set up a study group and Nordic Economic Cooperation Committee of officials to develop the proposals. The Committee, in consultation with ministers, presented a report in July, 1957 recommending a common market between the four countries covering eighty per cent of mutual trade and in September, 1957 a supplementary report regarding the remaining sector. The plans included proposals for a Nordic Investment Bank, for cooperation in fields of industrial production and for joint technical and scientific research. In November, 1958 the Nordic Council recommended to the four governments that, (20) Keesing's Contemporary Archives, 13620, 13656 and 13777. A number of references on following pages have also been derived from this source.
on the basis of the reports submitted, they enter into negotiations with a view to placing the matter before the parliaments when conditions permitted a decision to be taken. The formation of the European Free Trade Association, including Denmark, Norway and Sweden and to which Finland subsequently associated, has reduced interest in a Scandinavian customs union as a separate objective. However, the tenth annual session of the Nordic Council, meeting at Helsinki in March 1962, reached agreement on a convention providing for economic co-operation between Denmark, Finland, Iceland, Norway and Sweden. The convention was couched in the form of a programme declaration rather than of a document imposing formal obligations. The latter were avoided because of the negotiations taking place between most of the countries concerned and the Community.

(f) The Six

In September, 1947 French and Italian representatives signed a declaration setting up a mixed commission to study the possibilities for a Franco-Italian customs union. The commission's report, issued in December of that year, recommended the establishment of such a union over a period of four years and envisaged the ultimate participation of other countries. In March, 1948 the French and Italian foreign ministers signed a protocol defining the plan and programme for creation of the customs union between the two countries. The protocol provided for the appointment of a further mixed commission to prepare the agreement and the programme for its execution which would
be ratified by the respective parliaments. Although this project came to nothing it is noteworthy that M. Bidault, the French foreign minister, spoke at that time at a press conference of a customs union also comprising the Benelux countries and a democratic Germany which might reach an understanding with Britain safeguarding the traditional economic relations of the latter with the Dominions.

In November, 1947 France, Italy, the bi-zone of Germany and the Benelux countries signed a payments agreement, known as the Agreement on Multilateral Compensation. They were soon joined by a number of other European countries but these at first did not take a full part in the agreement.

The first attempt to form an economic union among the Six (France, Italy, the Federal Republic of Germany and the Benelux countries), took place at Luxemburg in November 1949. The scheme was known originally as FRITALUX, later as FINEBEL. It was agreed that the five (i.e. excluding Germany) should liberalise sixty per cent of their mutual trade (free this trade from import restrictions) and should not replace the restrictions by prohibitive customs duties. They would co-ordinate their financial and economic policies so far as possible and would seek to establish conditions for equal competition. The development of the scheme foundered on the political question of the inclusion of Western Germany, to which France was at that time opposed. Consequently, experts meeting to discuss the scheme in January, 1950 decided to refer the proposals to the wider European forum in which both this scheme and that for multilateral
compensation became to some extent developed.

The Schuman Plan forms the landmark in the economic integration of the Six. In May, 1950 the French cabinet approved a declaration proposing the creation of a single authority to control the production of coal and steel in France and Germany, open for membership to other countries. A common higher authority would modernise production and improve quality, supply coal and steel on identical terms to French and German markets, develop exports in common and equalise and improve the standard of living of workers. The negotiations, which commenced in June, 1950, and lasted for six months, were conducted by representatives of the Six. The treaty setting up a European Coal and Steel Community for a period of fifty years was signed in April, 1951. The common market for coal and steel was established over the period February, 1953 to February, 1958 by which all time all internal barriers to trade in coal and steel had been removed and external tariffs harmonised except in the case of France and Italy where harmonisation was not achieved until February, 1960. In December, 1954 as agreement was signed providing for a measure of cooperation with Britain through a Standing Committee of Association, which would examine ways and means to reduce trade barriers. (21)

(21) Further particulars of E.C.S.C. are contained in Chapter 9.
In May, 1955 the Benelux countries proposed to the other members of the Six further measures of economic co-operation. The objectives of the proposals were adopted at a meeting of the Six at Messina in June, 1955. A committee of government representatives and experts was set up under the chairmanship of M. Spaak to study a number of specific problems and prepare a report. These problems included the establishment of an overall common market free of trade barriers, the rhythm of its introduction, financial, economic and monetary aspects, escape clauses, a common labour market, a re-adaptation fund, absence of national discrimination and coordination of social policies. The report of the Intergovernmental Committee was adopted by the Six at Venice in May, 1956 and arrangements were made for the convening of an intergovernmental conference, opening at Brussels on 26 June to complete outstanding negotiations and to draft the two agreements recommended, one for a European Economic Community and another for a European Atomic Energy Community. By the 4 February, 1957 agreement had been reached on all matters except the overseas territories and the ownership of fissile material. Final agreement was reached on the 20th of that month and the two treaties were signed at Rome on the 25 March. After ratification by the parliaments of the Six the treaties came into force on 1 January, 1958.

In March, 1958 a European Parliament was established, providing a parliamentary institution for the two Rome organisations and also incorporating the Assembly of the European Coal and Steel Community, which had been in operation since September, 1952.
The common market for the Atomic Energy Community (Euratom) entered into full operation on 1 January, 1959.

On the same date the first steps were taken to remove trade barriers within the European Economic Community. Early in 1960 agreement was reached on the level of the common tariff (22) and in March, 1960 a programme of acceleration of the common market was devised so that this is now expected to be in full force at the latest by 1 January, 1970. In July, 1958 a conference on agricultural policy was held at Stresa but agreement on a common policy was not reached until January, 1962. This enabled the second stage of the Treaty to commence on the first of that month. (23)

In February, 1961 heads of State or Government of the Six met at Paris to discuss closer political union. Some diversity of views later appeared between President de Gaulle, who wished for political coordination of national states and that of M. Spaak, who desired a supra-national organisation which would ignore national identities. This question, despite some degree of compromise by M. Spaak, was still unresolved in August, 1962. It is also understood that some members of the Six wish to make political union conditional on British entry into the Community.

(22) Except for petroleum products
(23) Further particulars of E.E.C. are contained in Chapter 2 and of Euratom in Chapter 9.
(g) **Wider European economic cooperation**

Early post-war organisation in the field of overall European economic cooperation included the European Coal Organisation and the European Central Inland Transport Organisation. The functions of both these bodies were taken over by the Economic Commission for Europe, a regional economic commission of the United Nations. E.C.E. held its first session in May, 1947 and has continued to perform a number of functions. An important feature is the participation of Communist countries whereby it has had continually to tackle difficult tasks of cooperation between East and West.

Close economic cooperation in western Europe derives from the Marshall Plan for economic aid to Europe by the United States. The Paris Economic Conference of sixteen western European countries (Britain, France, Italy, Netherlands, Belgium, Luxemburg, Norway, Sweden, Denmark, Austria, Switzerland, Portugal, Ireland, Iceland, Greece and Turkey), which met from July to September, 1947, presented a report to Mr Marshall containing detailed proposals for a four-year programme of reconstruction by the participating nations. The report contained a statement to the effect that the conference had considered the desirability of establishing a customs union in Europe. This, it was stated, would lead to greater efficiency in production and would increase the wealth of the area. But Europe could not exist on its own resources so that no narrow solution could be found. Moreover, the problems involved,
such as those presented by the diverse stages of industrialisation in the area, would require patient study.

A Customs Union Study Group, set up during the conference, met at Brussels and Rome in November, 1947 and early 1948. This group favoured the method of union followed by Benelux and considered that smaller economic unions could pave the way for a European Customs Union. It gave some study to the problems of a common external tariff. Although the work of this body does not appear to have resulted in anything resembling a customs union, it was responsible for the preparation and acceptance of conventions on nomenclature and valuation and for the formation of the Customs Cooperation Council, which had promoted a number of important further measures for simplification of the customs procedures of member governments. This body has expanded beyond Europe and now includes Australia as a member. All sixteen countries represented at the Paris Conference participated in the study group and observers were present from the western zones of Germany, Australia, Canada, New Zealand, South Africa, India and Pakistan. This breadth of Commonwealth representation was not to be repeated when new proposals were discussed in later years.

The freeing of payments

The conference also set up a Committee on Payments Agreements which met at London in September 1947, and reported the following month in favour of setting up a central
organisation through which financial settlements would be made and whose task it would be to arrange at stated intervals a multilateral set-off of balances. The Agreement on Multilateral Compensation signed in November, 1947 comprised only the Six as full members but Austria, Denmark, Greece, Norway, Portugal, Sweden, Britain and the French zone of Germany soon adhered as occasional members. In the case of the full members set-off of primary balances was automatic but for the occasional members this required consent. Set-off of secondary balances, which involved payment by one country to another using the currency of a third country, always required consent, which was rarely given. All countries were concerned at the way dollar reserves left their hands and got into those of Belgium, which occurred because of the relatively strong financial position of the latter. (24)

Some improvement was secured by the Agreement for Intra-European Payments and Compensation of October, 1948. Primary compensations became automatic except for Switzerland and Portugal but secondary compensations still required consent. Because of her unfortunate experience in 1947, when she prematurely embarked on convertibility, Britain refused to make drawing rights, which were granted by creditor countries on United States insistence as a condition of dollar aid, transferable to other member countries unless the transaction was self-balancing. Patterns of trade thus continued to be frozen. (25)

Further progress was secured by an extension of the agreement in June, 1949, when funds were made available through United States credits to Belgium and Belgian credits to other members. But European debtors were still under the agreement induced to utilise seventy-five per cent of their drawing rights in particular countries. (26)

The devaluation of sterling in September, 1949 improved the position of Britain. In February, 1950 the Council of the Organisation for European Economic Co-operation (O.E.E.C.), the formation of which is discussed hereunder, approved general principles to govern future payments arrangements between member countries. As a consequence of this decision an agreement for a European Payments Union (E.P.U.) was drawn up, approved by the Council in July and formally signed by the member states in September, 1950. (27) The United States agreed to provide the working capital of the union. Each European member state was granted a quota commensurate with its economic importance. Its drawing rights and its gold deposits with the union were a proportion of its quota. At the monthly central clearings debtors and creditors received or provided settlements, either in gold or by credits. Balances up to the first twenty per cent of each quota were settled by credit, thereafter each "tranche" of twenty per cent attracted an increasing settlement in gold. During the life of the union the

(26) William Adams Brown, Jr. op. cit. page 321  (27) These now included the German Federal Republic and Thieste. The United States administration signed the agreement but Canada which, with the United States had become a member of O.E.E.C. in July, 1950, did not.
proportion settled in gold was twice increased. Important bilateral balances existing at the inception of the union were the subject of funding arrangements. Switzerland did not join the union until October, 1950.

In July, 1955 the Council of O.E.E.C. drew up a European Monetary Agreement to replace the E.P.U. when external convertibility was achieved by the main states. Under the E.M.A. the monthly clearing system continues but credits are not automatic but only by decision of the organisation. Moreover charges are imposed to encourage member states to effect settlements outside the mechanism of the agreement. Following the declaration of 27 December, 1958 of external convertibility by a number of western European countries, the E.P.U. ceased to exist and the E.M.A. came into being. During its history the E.P.U. was frequently called upon to afford special assistance to member states in difficulties. This included a credit of $120 millions to Western Germany in November, 1950, which country was later to become the main creditor in the union.

The O.E.E.C. and trade liberalisation

The O.E.E.C. came into being as a result of the Paris Conference which set up a working party to draft a convention for European economic cooperation. This convention was signed by representatives of the sixteen member countries as well as by the zone commanders. Article 4 of the Convention provided for efforts "to achieve as soon as possible a multilateral
system of payments among themselves and (the members) will cooperate in relaxing restrictions on trade and payments between one another, with the object of abolishing as soon as possible those restrictions which at present hamper such trade and payments. Article 5 provided for the members to strengthen mutual economic links and to continue the study of customs unions or analogous arrangements such as free trade areas, the formation of which might constitute one of the methods of achieving the objectives of the Convention. Members that had already agreed in principle to create customs unions would further the establishment of such unions as rapidly as conditions permitted. Article 6 provided that the members "would cooperate with one another and with other like-minded countries in reducing tariff and other barriers to the expansion of trade with a view to achieving a sound and balanced multilateral trading system such as will accord with the principles of the Havana Charter." (28)

A writer commenting on the inward-looking provisions of Articles 4 and 5 and the outward-looking provisions of Article 6 stated "the underlying assumption is clearly that the policies required by these articles are not only mutually consistent but reinforce each other. Under the circumstances prevailing when these commitments were first assumed, however, there were possibilities of conflicts between them. " (29)

(28) Of the International Trade Organisation. Although this instrument never came into force the majority of the provisions regarding trade have been incorporated into the G.A.T.T. (29) William Adams Brown, Jr. op. cit. page 309.
After discussing the temptations for the Europeans at that time to indulge in trade-diverting measures, the writer concludes that the convention "as a whole commits those countries to take the economic and technical steps necessary to ensure that American aid will contribute in due course to the emergence of such a (multilateral) system". (30)

On 1 January, 1959 the O.E.E.C. Council agreed to inaugurate a programme of liberalisation of trade between the member states. To start with, trade in products equivalent to fifty per cent of the value of total imports into each member state from other member states in a base period (generally the year 1948) was to be freed from import restrictions. Thus if in 1948 country A imported from other member states in the base period products q, r, s, t, u, v and w, it would have to freed completely from import restrictions say products q, r and w, the value of which was at least fifty per cent of total imports into that country from other states in 1948 or alternatively another group of products with equivalent value. In such circumstances the country was said to have achieved a fifty per cent liberalisation.

It has already been noted that at the end of 1949 France, Italy and the Benelux countries had been considering a form of economic union (FINEBEL) which did not materialise but that experts of these countries had suggested that the O.E.E.C.

(3) William Adams Brown, Jr. op. cit., page 310
be recommended to increase the liberalisation percentage to sixty. They also suggested that these members be asked to adopt as an objective the equalisation of protective and competitive conditions between them. In February, 1950 the O.E.E.C. Council decided to proceed with sixty per cent liberalisation and also made some decisions on the second recommendation. It was not, however, to accomplish much in the way of harmonisation of protective and competitive conditions. The Council at the same time resolved that member states proceed with the liberalisation of invisible transactions, a subject which has come up again on subsequent occasions and which is still being discussed by the successor to O.E.E.C. (O.E.C.D.) In 1951 seventy-five per cent trade liberalisation was achieved and in 1955 a ninety per cent level (with a minimum of seventy-five per cent in three categories of products - raw materials, foods and manufactures). There were some derogations of these requirements for member countries suffering serious balance of payments difficulties. (31)

Other O.E.E.C. schemes

In June, 1951 the French Cabinet approved the Pflimlin Plan for a European common market for agricultural products (the Green Pool), starting in the first place with wheat, sugar, dairy products and wine. Following a meeting at Paris in March, 1953 of the countries represented on O.E.E.C. it was decided to appoint an interim committee to draw up proposals to organise and unify agricultural markets. Britain was in favour of the proposal being transferred to O.E.E.C. whilst the

(31) Further comments on O.E.E.C. trade liberalisation are in Chapter 10.
Netherlands wished for the creation of a supra-national authority. In the event the Council of O.E.E.C. in January 1955 approved the transfer to O.E.E.C. of the Green Pool scheme and Spain, which had observed the Paris meeting, was invited to take part in the work of O.E.E.C. on agriculture. (32) A ministerial committee on Agriculture and Food was set up and in July, 1955 this Committee developed a programme for confrontation of national agricultural policies and for trade liberalisation. The annual reports of the Committee show that it is continuing its endeavours to promote the harmonisation of agricultural production in Europe. In July, 1955 Yugoslavia was also invited to be represented by an observer at O.E.E.C. meetings and as a member of technical committees.

Besides its work in the trade and agricultural fields the O.E.E.C. has also set up bodies to effect cooperation in the sphere of nuclear energy. In February, 1956 an ad hoc committee on nuclear energy was established and in the following July, a permanent steering committee to foster joint undertakings, prevent new trade restrictions and come to agreements with Euratom, which although then not formed, had been proposed. In February, 1958 there were established a European Nuclear Energy Authority to coordinate research and development plans and a Eurochemic Organisation, in which twelve member states participated, to establish plants to treat irradiated fuel.

(32) Spain became a full member of O.E.E.C. in July, 1959
The Stikker Plan (33) of June, 1950 to establish a European Integration Fund with the object of liberalising trade industry by industry, of making grants to modernise industry and for necessary investments, for a technical commission to report on industries and for coordination of budget policies, appears to have been too ambitious. About that time a coordinated plan for expansion and modernisation of European steel undertakings was indeed agreed upon but the purpose of this was in order to obtain necessary United States assistance for the industry.

Another ill-fated scheme was the Strasbourg Plan, approved by the Council of Europe in February, 1952, which had as its objects the development of overseas territories of the European powers, assurance of markets for the products of these territories in Europe and the development of processing industries in the territories. This apparently did not meet with the approval of the United States. The O.E.E.C. Council expressed opposition to the plan as being inconsistent with world-wide free trade and considered the scheme for a European Bank to develop the territories impracticable.

It is apparent that several of these unsuccessful projects, such as the second limb of the FINEBEL recommendations, the Dutch objective for the Green Pool, the Stikker and Strasbourg Plans, have influenced the content of the Rome Treaty for a European Economic Community.

(33) Heer Stikker, Netherlands Foreign Minister and Chairman of O.E.E.C, handed this plan to member states for consideration.
The reorganisation of the O.E.E.C.

In December, 1959 the four heads of state at the Western summit conference in Paris agreed, on American initiative, to hold an economic conference, which duly took place at Paris on 12 and 14 January, 1960. The countries attending were the United States, Canada, the Six (except Luxemburg), Britain, Denmark, Sweden, Switzerland, Portugal and Greece. The Commission of the European Economic Community was also represented.

The objects of the conference were threefold - the United States wanted the Europeans to shoulder more responsibility for economic aid to the under-developed countries, particularly because of its adverse payments position; to facilitate a reapproachment between the Six and Seven; to study the form of a reorganised O.E.E.C.

Committees were set up including an expert committee on the reorganisation of O.E.E.C. which reported in April, 1960. In May, 1960 a conference on this reorganisation set up a working party to draw up a draft convention and a meeting of ministers in July set up a preparatory committee to carry on this work, which was finalised in December, 1960.

The new body was called the Organisation for Economic Cooperation and Development. The Convention signed in December, 1960 is of a general nature and leaves much to be worked out in practice. The headquarters are at Paris. (34) The governing body is a council and there is an executive committee. (35) Binding decisions normally require unanimity

(34) Article 18. (35) Articles 7 and 9.
of all member states. The objects of the organisation are to promote economic growth, employment and a rising standard of living in member states while maintaining financial stability and to promote world trade and sound economic expansion in countries in process of economic development. The Convention contains no reference to discriminatory action. The members are to "pursue their efforts to reduce and abolish obstacles to the exchange of goods and services and current payments and to maintain and extend the liberalisation of capital movements." This is quite general in nature and not confined to member states. The objectives are to be achieved by mutual information, discussions, studies and close cooperation. The United States and Canada are full members.

The liberalisation programme of O.E.E.C. has been abandoned and G.A.T.T. was asked to intensify its efforts in that field. Rules on export incentives were also incorporated in a G.A.T.T. declaration. The O.E.C.D. has, however, its Committee of Trade. This carries out confrontations of the trade policies and practices of members in order to promote free exchange of goods and services. It also examines specific trade problems primarily of interest to members and their overseas territories and is concerned with the relationship between the Six and Seven. There is also a Development Assistance Committee which coordinates aid to under-developed countries. A number of O.E.E.C. committees and projects are continued including the ministerial committee on agriculture and food.

(h) The Community and other European countries

Following the adoption at Venice in May, 1956 by the Six of the report for the establishment of E.E.C. and Euratom, the Council of O.E.E.C. in July of that year decided "to study the possible forms and methods of association on a multilateral basis between the proposed customs union and member countries not taking part therein" and set up a working party for that purpose. (38) This body reported at the end of January, 1957. The report covered the problem raised by the definition of origin of products, the technical considerations involved in the removal of trade barriers and the special problems arising from the inclusion of the customs union of the Six. The report concluded that it was technically possible to operate a free trade area between the countries in question.

The industrial free trade area negotiations

At the end of September, 1956 the British Chancellor of the Exchequer (Mr Macmillan) and the President of the Board of Trade (Mr Thorneycroft) discussed the matter with Commonwealth Finance Ministers at their meeting in Washington. On his return to London Mr Macmillan issued a statement explaining that Britain had in mind an industrial free trade area excluding food, feeding stuffs, drink and tobacco. These exclusions were necessary both to protect British agriculture and to maintain the preferences given to the Commonwealth. This point of view was set out at some length in a statement circulated by Britain.

to members of O.E.E.C. in February, 1957. (39)

The Council of O.E.E.C. meeting later that month decided to enter into negotiations for ways and means to create a European free trade area associated with the common market of the Six. This instrument, it stated, should provide for expansion of trade in agricultural products on a basis of non-discrimination. The British Chancellor of the Exchequer and Chairman of O.E.E.C., now Mr Thorneycroft, was asked to place proposals before the Council for setting up the necessary working parties and to guide and coordinate their work. These were set up the following month. The first was to determine the conditions under which a European free trade area could come into being, the second examined agriculture and the third dealt with the special problems of industrially under-developed European countries, the "peripherals".

In May, 1957 the French expressed a desire for some delay in the negotiations pending progress in ratification of the Rome Treaties. (40) In mid-July it was reported that other O.E.E.C. countries could not accept the British view that agriculture should be excluded. (41) In August Britain appointed the Paymaster-General, Mr Maudling, to be responsible for their part in the negotiations. On 16 October Mr Maudling announced that Britain was prepared to enter into a parallel agreement on agricultural products. It would not reduce or abolish customs duties on these products but it did not object.

(39) This statement was published as a United Kingdom white paper, Cmnd.72. (40) Cmnd. 648 page 4. (41) The Observer, 14 July, 1957.
to such action by other countries nor would it expect to enjoy the benefit of such action. On the following day the O.E.E.C. Council decided to set up an Intergovernmental Committee at ministerial level on which all seventeen member countries would be represented, to carry on the negotiations. Under British chairmanship this became known as the "Maudling Committee".

In December, 1957 Britain circulated a draft agreement on agriculture which it revised the following month. (42) The draft was apparently not well received by the Six. (43)

The negotiations in the Maudling Committee were attended throughout by the development of divergent points of view on numerous matters. The French were particularly concerned at the likelihood of distortion of competition in the industrial field due to the different cost conditions confronting industry in the various countries. They were also concerned that Britain would have a disproportionate advantage in possessing the preferential access to two large markets, Europe and Commonwealth. The French developed plans for a sector-by-sector treatment of industry, for sharing of preferences and for harmonisation of social conditions, which were discussed by the Six. (44)

Very shortly afterwards, Signor Carli, Italian Minister for Foreign Commerce, produced an ingenious plan for harmonisation of external tariffs. (45) An upper and lower limit was to be set for the tariff on a given commodity, the gap between the two allowing for transportation costs from member state to member state. If a member maintained an external tariff lower than

the minimum level, other countries in the area would be allowed to levy a countervailing charge equal to the difference. The scheme rested upon the theory that relative costs of production are reflected in the relative tariff levels on the product in the different countries; an equalisation of tariffs would therefore tend to equate production costs. The negotiations considered the proposals useful though they were never accepted nor indeed fully worked out. (46) The failure to settle this problem was fatal to the negotiations. Although some progress was made on minor issues in the course of 1958, on 14 November, during the course of a meeting in Paris of the Maudling Committee, the French Minister for Information, who was not a member of the Committee, announced to the Press that it did not seem possible to the French Government to establish a free trade area as proposed by Britain and that they were looking for a new solution. (47) In the circumstances negotiations in the Maudling Committee were suspended.

Shortly afterwards it was reported that France and Germany were preparing a plan to extend to other members of the O.E.E.C. the benefit of certain tariff cuts to be made between the Six on 1 January, 1959. (48) The plan, as approved by the Six on 3 December, provided for a unilateral cut of the external tariffs of the Six by ten per cent in favour of all countries.

that were members of the G.A.T.T. In no case, however, was the cut to bring any rate below that proposed for the common tariff. (49) The possibility of some reciprocal extension to other members of the O.E.E.C. of the quota expansions scheduled to take place amongst the Six was discussed in the Council of O.E.E.C. A refusal by the French to offer the full benefit of this expansion to other O.E.E.C. countries led to talk of reprisals by the British delegate and to a walk-out by the French delegate on 15 December. (50) However, Franco-British negotiations were initiated in 1959, covering in particular products where quotas were nil or negligible in size. Under the Rome Treaty quotas equal to three per cent of national production were established in the first place in this sector. (51) A trade agreement between the two countries signed on 2 April 1959 showed a twenty per cent increase of existing quotas with some special arrangements in the 'nil or negligible' sector. (52) No similar agreements between members of the Six and other members of O.E.E.C. have been reported.

The European Free Trade Association

Following reports in November, 1958 that a free trade area was being discussed (53) and in March, 1959 that there had been a meeting at Stockholm in this connection (54), formal proposals were put forward by Sweden in May, 1959 for a "little free trade area" of the "Seven" (Britain, Austria, Denmark, Norway, Portugal,

Sweden and Switzerland. (55) Following a meeting of officials in June at Stockholm in order to draft a plan (56) ministers on 21 July at Stockholm agreed to go ahead with the establishment of a European Free Trade Association. Their communiqué stated that they wanted early negotiations with the Six and that officials had been instructed to draft a convention in accordance with a plan attached. (57) The convention was initialled at a meeting at Stockholm in November, 1959, ratified by the national parliaments early in 1960, instruments of ratification being formally deposited at Stockholm on 3 May of that year.

The convention provides for the elimination of tariffs and quantitative restrictions on industrial goods on trade between the Seven over the period 1960 to 1970 and for the conclusion of special agreements on agriculture. Agricultural agreements have been made between Denmark and Britain, Austria, Sweden and Switzerland and between Portugal and Switzerland. Britain has also concluded an agreement with Norway on certain fish items.

In March, 1961 Finland signed a treaty of association with E.F.T.A. which makes her in effect, though not formally, a member of the association. On a few products Finland (as was the case with Portugal) is allowed to delay tariff reductions and she may also temporarily maintain import restrictions on certain fertilizers, petroleum products, coal and coke. Finland has also signed an agricultural agreement with Denmark. (58)

(56) The Economist Intelligence Unit, Spotlight, 19 June, 1959.
(i) Expansion of the Community

An agreement between the European Economic Community and Greece creating an association was arranged in March, 1961 and came into force on 1 November, 1962. The agreement provides for a customs union to be brought into being over a transitional period. There are a number of protocols annexed which take account of special aspects of the Greek economy. Provision is made for financial assistance to help Greece to speed up its economic development and to raise the standard of living of its people as rapidly as possible. At a later date, when its economic progress allows, it is intended that Greece become a full member of the Community, accepting all the obligations of the Rome Treaty. A request of Turkey for association has been the subject of discussion over a number of years; discussions have also been taking place with Israel and Iran.

Meanwhile a strong political movement gathered force in Britain in favour of joining the Community. In the Council of Western European Union (59) the British Foreign Secretary, Mr Selwyn Lloyd, stated in June, 1960 that, whilst Britain could not join the common market in its present form, she was prepared to examine ways of establishing closer cooperation with it in some form of qualified membership. It was in this context that Britain had applied to join E.C.S.C. and Euratom. (60) This offer was not enthusiastically received by the Six, perhaps

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(59) An organisation composed of representatives of the Six and of Britain, formed to discuss defence policy. (60) An offer made in the Assembly of W.E.U. by a British spokesman some months previously.
because eventual amalgamation of these two bodies with E.E.C. is planned. (61) In February, 1961, Mr Heath, Lord Privy Seal, at a meeting of the same body, offered a common or harmonised tariff on raw materials and manufactured goods imported from countries other than the Seven or Commonwealth, special arrangements for tropical products and stated that Britain would see no difficulty of principle in the way of discussion between the Six and Commonwealth countries about possible reductions in the tariff preferences now enjoyed by Britain in those countries. (62)

In April, 1961 it was reported that President Kennedy was throwing his weight behind the concept of British association with the Six. He "appears to be more concerned with strengthening Europe politically and economically than with attempting to preserve United States exports from the effects of a customs union". (63) Following his visit to Washington about this time, Chancellor Adenauer publicly advocated British membership of the Community.

The following month Mr Macmillan spoke in Parliament anticipating full membership or association for Britain and a few days later Mr Heath indicated how far Britain could go. Early in June Mr Macmillan emphasised that no decision had been taken but shortly afterwards Lord Home, Foreign Secretary, advocated entry into the common market and commented that Britain would have a hand in deciding and controlling the political implications. As the latter had been generally considered the

main obstacle to British membership, this was significant.

Later in June three ministers were sent to tour the Commonwealth and discuss the matter with Commonwealth governments, Mr Sandys, Commonwealth Relations Secretary, was sent to Canada, Australia and New Zealand; Mr Hare, Minister of Labour, to Africa and Mr Thorneycroft, Aviation Minister, to the Asian members of the Commonwealth. The communiqués showed that many countries, including Australia, were concerned at the implications for their interests of British membership.

Nevertheless, the British Government made formal application to initiate negotiations to see if satisfactory arrangements could be made for her to join the Community on 10 August, 1961. Ireland applied for membership at the same time and later applications were submitted by Denmark and Norway. Austria, Portugal, Spain, Sweden and Switzerland applied for association.

Discussions between Britain and the Six are proceeding but agreement has as yet not been reached. It appears that some measure of understanding has been reached that Commonwealth preferences on manufactured goods will be phased out over the transitional period so that they cease to exist by 1970 but that in the case of India, Pakistan and Ceylon preferences on some manufactures will be only reduced provided the volume of trade is maintained. It is also understood that some members of the Commonwealth will seek association and that the British overseas territories will also be associated. Ghana, Nigeria and Tanganyika have, however, made it clear that they do not wish
to be associated; nevertheless they are seeking arrangements that will preserve their trade.

Generally speaking the Commonwealth has not been able to take part in the negotiations between Britain and the Six. An Australian official, Dr Westerman, secretary of the department of Trade was, however, enabled to address the committee of deputies of the Council in Brussels on 26 April, 1962 and to present in detail proposals sought for safeguarding Australian trade interests.

In September, 1962 the Prime Ministers' Conference in London devoted most of its time to reviewing the progress made in the negotiations in Brussels regarding the conditions on which Britain might join the E.E.C. and to examine the nature and prospects of safeguards for the trade of Commonwealth countries. Commonwealth representatives drew attention to the difficulties to which developments could give rise in relation to their trade with both Britain and other countries. They explained the extent to which their interests had so far not been met in the negotiations. However only when the full terms were known would it be possible to make a judgement. (64)

(j) Economic Integration in Eastern Europe

As a result of the second world war, Soviet Russia obtained an ascension of influence in eastern Europe and was able to impose communism on a wide area which became subject to her political influence. There were numerous territorial changes such as the absorption by Russia of the Baltic countries, East Prussia and part of Poland, the boundaries of which were shifted (64) Communique of 19 September, 1962
westwards into Germany. The following countries became satellite states of Russia - East Germany, Bulgaria, Czechoslovakia, Hungary, Poland, Roumania, Albania and Yugoslavia. The latter two countries, although remaining communist, have more recently drifted from the Soviet orbit. Russia also gained special trading rights in Finland which complicated the association of the latter with E.F.T.A. and political rights in Austria, which prevent this country from being a member of E.E.C., a position also shared by Finland.

There has been a considerable measure of economic integration in eastern Europe. This is effected through the Council for Mutual Economic Assistance (COMECON) formed in 1949. This body provides an instrument for maximising trade between Russia and the satellites and also undertakes industrial planning to ensure that there is industrial specialisation within the bloc. At its meeting in Tirana in May, 1959 COMECON planned for mutual expansion of trade by seventy per cent between 1958 and 1965. This is a rate of expansion well below that achieved in the 1950's and it may well be exceeded. (65) With complete state control over trade and an artificial system of pricing there is a tendency for the bulk of the trade of satellite countries to be effected through bilateral quota agreements. The existence of COMECON and associated political pressures has directed a high proportion of this trade to other eastern countries. Czechoslovakia's external trade, for example, in 1958 was directed as to seventy one per cent to other COMECON countries, a percentage expected to increase to seventy five by 1965 (66).

II. THE EUROPEAN ECONOMIC COMMUNITY AND EUROPEAN FREE TRADE ASSOCIATION

The European Economic Community

(a) Background and description

Chapter 2

(i) Background

The reasons for the formation of the European Economic Community were both political and economic. As in the case of the Zollverein, there is no doubt that the political considerations were at least as important as those with an economic motive. The first real move towards integration of the Six, the Schuman Plan, was indeed widely hailed as a move towards resolving the political enmities of Germany and France rather than a move towards greater economic prosperity.

However in the modern age when the development of all-too-powerful weapons has put armed conflict a little further into the background, the problem of defence is not thought of as purely a political one but as an economic problem as well. The attainment of as high a level of prosperity and technical efficiency as one's neighbour is important to the maintenance of prestige in world fora and enables a country to play a more adequate part in assisting in the development of the retarded areas of the world. Moreover an efficient economy is a prerequisite for efficient defence.

The view is now widely held that many national units are too small to generate sufficient economic growth
and that economic strength and expansion are now likely to be achieved through the grouping of these units. (1)

In the case of Germany there had been in the years preceding the Messina Conference a rapid expansion of industrial growth and exports. The increase in exports, insofar as other European countries were concerned, was somewhat of an embarrassment as heavy payments deficits were being regularly experienced by those countries and gold balances were being accumulated by Germany in the European Payments Union. It is apparent that any stimulus to the economic efficiency of the other leading western European countries would tend to maintain German's exports and avoid measures that might otherwise have to be taken by those countries to restrain import demand. On the other hand the German agricultural sector was high-cost and highly protected and there was some determination that the Green Plan for development of this agriculture should not be impaired by opening the German market to agricultural imports. The form of the agricultural provisions of the E.E.C. Treaty, of the common agricultural policy developed to implement these and of the relatively high price levels determined for initial operation of this policy result largely from German interests and the justification for these is political rather than economic.

On the industrial side there was a high degree of resistance in Germany to taking measures to improve the real

earnings of the workers and to afford them more leisure and social benefits. These measures were an inevitable accompaniment of integration. They would indeed help to solve the intra-European balance of payments position but they would render Germany less competitive in markets outside Europe, notably the United States. The economic balance seems, therefore, to have been rather against German participation in full economic union and in fact the Economic Minister, Dr. Erhard, was reluctant that this step should be taken. The decisive impulse to participation came from the political side and, notably from the Chancellor, Dr. Adenauer.

France has always been in the forefront in promoting economic integration. Whereas the name of Schuman is primarily associated with economic integration for political ends, that of Monnet is rather associated with economic integration for its own sake. Despite French enthusiasm for the concept, France has been a very hard bargainer. Insofar as the Rome Treaty is concerned, the effect of France's demand is clearly seen in the provisions regarding association of overseas countries and territories and in numerous provisions designed to harmonise competitive conditions in the Community. These provisions include those providing for equivalence of social charges, equal pay for men and women, and so on. Moreover, to France may be attributed the concept in the common agricultural policy that members of the Community with a need to import foodstuffs should primarily import these from Community partners at prices equivalent to prices guaranteed
to domestic producers. The earliest expression of the agricultural policy, the Franco-German grains agreement, gave concrete expression to this principle.

In the various negotiations with Britain, France has also been prominent in its insistence on certain conditions. It has been disturbed at the advantages that would accrue to Britain if it possessed a large preferential market outside the Community, not shared by other members. It has been concerned at the cost advantages accruing to British manufacturers if they can continue to obtain raw materials duty free from Commonwealth sources and at the likely labour cost advantages if cheap foodstuffs continue to enter duty free from these sources and if British agriculture continues to be protected by subsidy as this also results in cheap foodstuffs and makes it difficult for France to penetrate the market for foodstuffs except by itself subsidising exports to Britain.

However, to describe France's exigencies is not to indicate the economic advantages she saw in integration apart from the possibility of expanding her exports of foodstuffs at prices showing a sufficient return and sharing the costs of developing her overseas territories. On the industrial side the economic advantages appear to have included a belief that industry in France could be expanded and put on as sound a basis as that in Germany if conditions of competition were harmonised. Moreover France's markets for high-class products which tended to be restricted by high barriers could
be greatly expanded. These concepts are a considerable departure from France's traditional attitude which has been one of self-sufficiency, a minimum of export trade being developed sufficient to pay for imports which could not be produced in the French Community. Generally speaking most imports were obtained from the overseas territories of the French Union and preferential devices assured that the requirements of the territories for manufactures were obtained from the home country. To what extent the proximate break-up of the French Union was contemplated and was consequently a factor in changing French concepts on trade is not apparent.

In the case of Italy and Benelux it is equally difficult to isolate purely economic as distinct from political reasons - including defence - for their desire to join the Community. In the case of the Netherlands there was an attraction to the concept in the prospect of expanding markets for livestock produce but a distrust of the aspect of the agricultural policy which would oblige them to purchase food grains from France at relatively high prices rather than retain access to supplies at the cheaper world price. The provisions in the Treaty for duty-free tariff quotas reflect Netherlands needs in this respect. Netherlands fears at the impact on its competitive ability have diminished with the increasing prospects of British membership. Italy has also been attracted by better prospects for its agricultural exports whilst concerned about the impact of integration on its less efficient branches of agricultural production.
In the case of all these countries the economic attraction on the industrial side appears to have been similar to that in France. In other words, these countries felt that they could become, with certain safeguards, competitive with Germany and that the larger market and stimulus of competition would assure a higher rate of economic growth.

As one author put it, "the size of the market is a problem of which Italians are becoming vividly aware. In spite of the high rates of increase of production and exports after the war, the need to overcome the limitations of the domestic market is being sharply emphasised by the constant advance of modern production techniques and by the fact that other countries are favoured when competing with Italy by the large size of their domestic markets. Such limitations are now regarded as a serious obstacle to a full development of the national economy, and this widespread belief is expressed, in particular, by Italy's readiness to join in the various endeavours towards international economic integration which have recently led to the establishment of the European Economic Community". The initial stress by this author on the size of the market is somewhat reduced in emphasis when he proceeds to point out that the Italian population is comparable in size to that of Britain, Germany and France, which have progressed much further and when he transfers the emphasis to the beneficial effect increased competition is likely to have in

(2) V. A. Marston in 'Economic Consequences of the Size of Nations' (E.A.G. Robinson, editor), 1960, page 151. This may be contrasted with views of economists in the following chapters of this thesis.
reducing the existing monopolistic and oligopolistic structure and in assuring the adoption of up-to-date techniques.

However, it is a fact that Italy does possess some industries, such as the motor-car industry, which could benefit by the removal of trade barriers.

In the case of Belgium, economic integration has long possessed attractions because of the way the economy of such a small country has been buffeted between the divergent impulses it has received from abroad. Between 1924 and 1932 Belgian wages kept in line with French wages; from 1935 to 1938 they followed British wages and from 1949 to 1955 American wages. One author remarks that however astute a small country's economic policy may be, it will never enable that country to escape the disturbances imposed upon it by the lack of co-ordination in the policies of the great powers. Any alignment with one or the other group tends to become so complete that the economy of the small country swings either all one way or the other. Sales may have to be transferred from one market to another and among groups of products. It is difficult to stabilise the flow of business, long-term industrial risks increase and also obstacles to a balanced growth of production. Belgium has for a long time depended on export markets and has followed a low tariff policy. The formation of the Community must have appeared for Belgium as a logical extension of the steps she had entered into first in forming the Belgo-Luxemburg economic (3) L. Duquesne in Robinson op.cit. page 81.
union and secondly Benelux. Moreover the agricultural policy of the Community must have been welcome to her in view of the difficulties she had been encountering in harmonising her agriculture with that of the Netherlands in the context of Benelux.

In all these countries fears of submergence of local industry by German competition appear to have been allayed by the assurance of a high degree of industrial combination across the whole area of the Community.

(2). Description of the European Economic Community.

(i) The Customs Union.

The Rome Treaty establishing a European Economic Community between the Six consists of a preamble, six Parts and a number of Annexes.

The preamble is general in nature and it is necessary to look to Part I of the Treaty, which deals with "Principles", to find that it is the "aim of the Community, by establishing a common market and progressively approximating the economic policies of the member states, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increased stability, an accelerated raising of the standard of living and closer relations between its member states."(4) Moreover, for these purposes the activities of the Community are to include, inter alia, "the elimination as between member states of customs

(4) Article 2.
duties and of quantitative restrictions in regard to the importation and exportation of goods, as well as of all other measures with equivalent effect" and "the establishment of a common customs tariff and a common commercial policy towards third countries." (5)

These activities, with the exception of the common commercial policy, are regarded by the General Agreement on Tariffs and Trade (G.A.T.T.) as the essential aspect of a customs union. (6) Part Two of the Rome Treaty sets out in Title I, under the heading "Free Movement of Goods", the detailed provisions relating to the Customs Union. Before proceeding to an examination of these provisions it may be noted that Article 8 in Part One provides that

"the common market shall be progressively established in the course of a transitional period of twelve years." This transitional period is divided into three stages of four years each and to each stage is allotted a group of steps to be taken and pursued concurrently. In certain circumstances the length of the stages may be extended but not so as to have the effect of prolonging the transitional period beyond a total duration of fifteen years from the date of entry into force of the Treaty. The first stage in fact ended on time so as to enable the second stage to commence on 1 January, 1962. The second and third stages may also be curtailed by decision of the Council by unanimous decision. The Council is a body comprising one minister from each of the Six.

(5) Article 3. (6) Article XXIV of the G.A.T.T.
The introductory section of Title I makes it clear that the Community provides for free circulation of goods originating outside as well as inside the Six. (7) However, certain rules will apply to such external products which may not be subject to drawback when exported by one member state to another. (8).

Chapter 1 of Title I is headed "The Customs Union"; Chapter 2 "The Elimination of Quantitative Restrictions as between member states". Generally the latter is considered a feature of the former, the differentiation in this case possibly reflecting a logical view that a custom union is only concerned with customs duties.

Section 1 of Chapter 1 provides for the elimination of customs duties as between member states; this is also expressed to cover charges in force having equivalent effect. No new import or export duties are to be introduced on trade between member states. Import duties are to be abolished over the transitional period by means of successive reductions to a basic duty which is defined as that applied on 1 January, 1957. The first reduction of ten per cent is scheduled for 1 January, 1959 and applies to all products. It was in fact effected at that time. Subsequent reductions were scheduled according to a formula leaving some latitude as to the extent of the reductions applied to the duty on any given product at the time of each reduction. The general effect must, however, amount to an average reduction of thirty percent in the first stage, a further thirty percent in the second stage (9).

(7) Article 9. (8) Article 10. (9) On the average, customs duties are to be reduced by sixty percent from their 1957 level during the first two stages.
whilst during the course of the third stage all import duties are to be completely abolished on internal trade. Member states may suspend in whole or in part the collection of customs duties on trade of other member states and may reduce such duties more rapidly than scheduled. (10) Some acceleration has in fact been carried out. By 31 July, 1962 customs duties had been reduced by 50 percent for industrial products, 35 percent for non-liberalised agricultural products and 30 percent for liberalised agricultural products. Export duties on internal trade were scheduled for abolition by the end of the first stage. (11) Customs duties of a fiscal nature were separately treated in calculating the reduction of total duties. These duties are also to be progressively reduced, though permission may be obtained to retain them for a period of up to six years. Moreover, they can be replaced by an internal tax. (12) In fact several cases of substitution of customs duties on items such as coffee, by internal taxes, have been reported.

Section 2 deals with the establishment of the common customs tariff. The general principle adopted is that the duties under the common tariff shall be at the level of the arithmetical average of the duties applied in the four customs territories covered by the Community. (13) There are, however, numerous cases where other principles obtain. In some of these cases special rates have been fixed by agreement, either in the Treaty or subsequently. In many of such cases the reason for fixing special rates is that one or more of the member states

has an industry for which it demands a certain degree of protection not hitherto afforded by the other member states, which may not possess a similar industry. Thus Italy is the only member state with substantial tariffs on lead and zinc and special duties were fixed on these metals in accordance with the Treaty. The common tariff is to be brought into force in three steps, one at the end of each stage. (14) Thirty percent of the difference between the existing individual tariff and the common rate is to be added or subtracted, as the case may be, by the end of the first stage, a similar adjustment is to occur at the end of the second stage and the remaining forty per cent is to be adjusted before the end of the transitional period. Where in any case the difference is very small, not more than 15 per cent of the rate in the common tariff, this tariff will be fully applicable by the end of the first stage. There are provisions for temporary suspension of customs duties in certain circumstances with the permission of the Council, which suspension may be limited to a defined quota of imports. This provision has been used on several occasions. In the case of tropical timber the use of tariff quotas met with objections from the associated countries and the tariff quotas approved had to be modified. Any member state is allowed to accelerate adjustment of its external tariff towards the common tariff.

(14) The first general move towards the common tariff was made on 1 January, 1961. Except for some particularly sensitive items the move was made on the basis of the common tariff as fixed, less twenty percent. This was in anticipation of cuts in the common tariff of up to twenty percent in G.A.T.T. negotiations.
Chapter II prohibits the introduction of new quantitative restrictions on trade between member states and provides for the abolition of export restrictions by the end of the first stage. Import restrictions are to be abolished by means of a formula providing for the grouping of quotas and for the annual expansion of these grouped quotas until such time as they are so large as to have no restrictive effect; when the restrictions are to be abolished. Thus, Italy may have an existing quota for cotton sheeting from France, Germany and Benelux. These quotas will be combined and the combined quotas will be available for imports from all three countries and will be increased annually. The importance of these provisions is not so great as at first sight appears because of the large number of industrial products already freed from restriction under the O.E.E.C. liberalisation programme. Moreover, during the first four years of the Community's existence, an appreciable part of the non-liberalised sector was outside the scope of the general rules, either because of the existence of a state monopoly or marketing organisation or because of the introduction of a minimum price system.

Probably the most important provision in regard to expansion of quotas is the one that provides that where previously existing quotas were nil or negligible, quotas were to be established on 1 January, 1959 at not less than three per cent of national production, rising to five per cent by 1 January, 1961 and thereafter increasing in size by fifteen per cent annually. This affects certain very highly protected

(15) Article 33.
branches of industry, such as motor car manufacture, especially in France. There are also provisions requiring state commercial monopolies to operate so as to exclude discrimination between the products of member states. (16) Some progress has been made in authorising state monopolies to import goods such as tobacco from other member states.

(ii) Agriculture

The Rome Treaty provides that the common market shall apply to agriculture and trade in agricultural products. (17) There are, nevertheless, a number of special provisions in the Treaty regarding agriculture and also a general proviso that "the common organisation" of agricultural markets may comprise all measures necessary to achieve the agricultural policy objectives, including in particular, price controls, subsidies as to the production and marketing of various products, arrangements for stockpiling and carry-forward and common machinery for stabilising importation and exportation. The arrangements are to exclude any discrimination between producers or consumers within the Community. (18)

The objectives of the common agricultural policy are to increase agricultural productivity by developing technical progress and by ensuring the rational development of agricultural production and the optimum utilisation of the factors of production, particularly labour, - to ensure thereby a fair standard of living for the agricultural population, particularly by increasing the individual earnings of persons engaged in agriculture - to stabilise markets - to guarantee

regular supplies and to ensure reasonable prices in supplies to consumers. (19)

The "common organisation" of agricultural markets which is to be developed to achieve these objectives may take one of three forms, depending on the product —

(a) a European marketing organisation,
(b) compulsory coordination of the various marketing organisations,
(c) common rules regarding competition. (20).

The nature of the common rules is not revealed by the Treaty. The regulations that have now been adopted regarding vegetables and fruit and wine give some indication of the nature of such rules.

The Treaty provides for two interim methods of development of trade between the member states. One of these, "minimum prices", is a method of limiting competition and may possibly be used beyond the transitional period. (21) The other, "long-term contracts", is a device for directly promoting trade between the partners. The method of "minimum prices" has been used by individual members of the Six for a number of years against relatively cheap imports. Italy has employed these on butter and meat. Within Benelux, Belgium has used this against imports from the Netherlands of dairy products and meat. France has used this system to protect her production of poultry, pigmeat, potatoes and a number of fresh fruit and vegetables. (22)

(19) Article 39(1). (20) Article 40(2)
The method of long-term contracts, on the other hand, has been developed to assist member states to export at prices uncompetitive by world standards. It has within the Community, only been used to date to ensure the sale of wheat and coarse grains from France to Germany.

The Treaty defines "minimum prices" as being those below which imports may be temporarily suspended or reduced or made conditional on their price being above the minimum price fixed for the product concerned. (23) The first method appears to be that used by Italy, where certain products would not be imported if the domestic market price fell below a specified minimum. The second method, used in Benelux, is to levy an export tax to bring the export price of the product to the partner up to the specified minimum.

In regard to long-term contracts the Treaty provides for the quantities to be based on the average trade in the years 1955/7 and to progressively increase. The price also is to increase progressively up to the domestic price of the importing partner. These principles were used in the France-German Grains Agreement.

Both minimum prices and long-term contracts are now of little more than academic interest since the development of the common agricultural policy which certainly uses both conceptions of "minimum prices" in its framework.

The Treaty provided for the holding of a conference to formulate the general lines of the agricultural policy. (24) This was duly held in Stresa in July, 1958. It also provides (23) Article 44(1) (24) Article 43(1)
for the Commission to submit to the Council proposals concerning the working out and putting into effect of the policy. Guided by the Stresa decisions of principle the Commission submitted its proposals to the Council in December, 1959 (25) and following extensive discussions these proposals formed the basis of agreement on 14 January, 1962, on the outlines of the common agricultural policy.

From the end of July 1962 the common policy was introduced for grains, pigmeat, eggs and poultry to which a levy system is applied and for vegetables, fruit and wine to which is applied a system of common quality standards. As from the same date common criteria were introduced to fix minimum prices and rules to counter distortion of competition.

The system of variable levies is a complicated one and varies as between products. For instance, during the transitional period each member state will set target prices for wheat and producers will be supported by purchase of their wheat at prices closely related to the target prices. Imports from non-member states will be subject to a levy equal to the difference between world market price and the target price plus a further element called a "montant forfaitaire". Imports from non-member states are subject to the same levies without the "montant forfaitaire". Exports of member states both to other member states and to non-member states are made at world market prices; the difference between target price and world market price is paid to the member state out of a common fund.

The differences between national target prices in the member states will be progressively reduced over the transitional period and a common E.E.C. target price applicable to a single market centre is to be reached by 31 December, 1969 at the latest. The montants forfaitaires will be fixed annually and will disappear at the end of the transitional period by which time trade between member states will be free of levy or subsidy. The inducement to the consumer to purchase Community wheat after the end of the transitional period will apparently be that the local price will be rather below the target price at which the wheat can be imported. There will be a system of import certificates valid for three months, the issue of which will normally be automatic but which can be cut off in an emergency.

The above system, the description of which is somewhat simplified, will be applied with variations to the other grains, pigmeat, eggs and poultry. No target prices will however, be set for pork, poultry and eggs and levies on imports will be based primarily on differences in feed grain prices between importing and exporting member states in the transitional period and in the case of imports from outside countries on differences between world prices for feed grain and prices in the importing member state. The levies will contain an additional protective element during the transitional period to afford preferences to other member states. There will also be cut-off prices, which are minimum prices for imports before payment of levy and are obtained by applying a conversion
rate to the price of feed grains. If prices offered are less than the cut-off prices, the levy will be increased by the difference. On these commodities, unlike the case of wheat, exporters can avoid some of the charges by guaranteeing that they will not export to the Community below the cut-off price, c.i.f. the frontier. If the various measures are ineffective as protection the Council may decide on supplementary measures, such as import restrictions.

Fruit and vegetables must all be graded "Extra", 'Grade I" and "Grade II" for trade between member states. Import restrictions on "Extra" grade have been abolished and duties are to be eliminated by 1969. Restrictions and minimum prices are to be abolished on Grade I as from 1 January, 1964 and on Grade II as from 1 January, 1966. Safeguard measures, if necessary should be taken on low-quality fruit. Imports from non-members must also be graded and are subject to tariffs and to a form of minimum price or cut-off price. If the price of imports falls below this level, imports may be restricted or appropriate levies charged.

On wines there are to be quality controls not yet fully worked out. In the transitional period quotas will be opened and expanded for trade between member states. There will be tariffs on imports from non-member countries. Other methods of control are not yet specified.

The policy for beef and veal has not yet been finalised but it is proposed that guide prices be fixed in member states and that tariffs on trade between these states be phased out
over the transitional period. The guide prices will be adjusted so as to reach a common level by April, 1966. For imports from outside countries there will be cut-off prices with associated levies and also a common tariff of 20 per cent. (26).

The policies proposed for dairy products are roughly similar to those applicable to grains. A special feature is that domestic sales prices may be reduced in times of glut. (27)

The system of protection is thus a thorough one but it still remains to be seen at what level prices will be fixed when the common market stage is reached. This is crucial in determining how protective the system as a whole will be.

The common agricultural policy includes proposals for the creation of a European Agricultural Guidance and Guarantee Fund. This fund is to cover subsidies on exports, intervention on the national market and measures to improve agriculture, including structural changes. Contributions to the fund will be at first related to the scale of contributions to the budget of the Community but will be varied so as to depend increasingly on the proceeds of import levies.

On products where no levy has been fixed, minimum prices may be retained for one year but will be on a uniform basis throughout the Community.

(27) Cornish and Carrington, op. cit. page 85.
(iii) Association of Overseas Countries and Territories

The provisions of the Treaty regarding associated countries and territories are contained in Part Four and in an Implementing Convention annexed to the Treaty. The latter covers the period 1958-1962 only and the terms of a new convention are currently being negotiated. The Treaty contains provisions regarding tariff treatment whilst the Convention contains those on quantitative restrictions, the development fund and the right of establishment. (28)

The list of territories associated under these provisions does not include those which had attained independence prior to the Treaty such as Libya, Morocco, Tunisia, Laos, Cambodia and Viet Nam. The possible association of these states is covered by Declarations of Intention annexed to the Treaty but so far none of these countries have become associated. However Surinam has recently become associated but difficulties still remain to be resolved regarding association of the Netherlands Antilles. As a number of the territories associated under the Treaty have since become independent but have continued their association there are now eighteen associated countries and a few remaining French colonies associated, including New Caledonia. Guinea on attaining independence discontinued association and West New Guinea has become disassociated following political changes. (29)

(28) The French overseas departments are only treated as territories for purposes of the Development Fund and the right of establishment. (29) Algeria, formerly subject to the same regime as the overseas departments must now be considered as an associated country.
In regard to customs duties, the general principles of the Treaty regarding reduction and abolition of import duties, but not of export duties, apply as between the member states and the associated countries and territories and between the latter, with an important exception. The countries and territories are entitled to levy customs duties which correspond to the needs of their development and to the requirements of their industrialisation or which, being of a fiscal nature, have the object of contributing to their budgets. The duties in question are to be progressively reduced to the level of those imposed on imports of products coming from the member state with which each territory has special status. (30)

The provisions applicable to the liberalisation of import restrictions in the first five years are analogous to those applying between member states. There are certain differences in regard to the establishment of quotas by the territories on products in which the trade is now nil or very small and in the globalisation of quotas, from which the quota extended to the member state with which the territory has special relations is excluded. (31) The Development Fund provided for in the Convention is to be raised and spent in the five years. The principal beneficiaries are the former French territories. Allocation to projects is approved by the Council and their use for the approved purpose is verified by the Commission.

A number of criticisms have been levied specifically at the provisions of the Rome Treaty relating to overseas territories.

These criticisms have occurred not only in the G.A.T.T. but also in other organisations such as the Economic Commission for Asia and the Far East, whose members fear that their interests may be affected.

(iv) Other Treaty provisions

Title III of Part Two comprises provisions regarding the "free movement of persons, services and capital". Workers are to be entitled to move freely between countries of the Community to accept offers of employment actually made and to continue living there after being employed. There is to be no discrimination as to wages and working conditions on account of nationality. (32) Social security legislation is to be adapted to facilitate the receipt of benefits by migrant workers. (33) It was decided to implement regulations regarding social security for these workers as from 1 January, 1959 and this facilitated the implementation in September, 1961 of the first regulations on movement of labour. Under these regulations a preference for domestic workers in filling vacancies is initially to be maintained but any additional vacancies will in preference be offered to workers from other member states. The preference for domestic workers is to be gradually abolished. In regard to non-wage earning activities, restrictions on the freedom of establishment of nationals and companies of one member state in another member state are to be progressively abolished. (34) A general programme was adopted in December, 1961 for the progressive elimination of restrictions according to the degree to which

the activity in question is considered to constitute a contribution to the development of production and trade.

Restrictions on the free supply of services within the Community are also to be progressively abolished (35), the afore-mentioned general programme also dealing with this matter.

The movement of capital is to be freed subject to the liberty to take protective measures if disturbances to the functioning of the capital market arise. (36) A directive was issued by the Council in May, 1960 specifying the range of capital movements to be unconditionally freed, those to be liberalised conditionally and those on which no agreement had at that stage been reached. In June, 1961 the Commission made recommendations to Governments with a view to greater flexibility of the national regulations. The degree to which freedom of capital movements is implemented qualifies the right of establishment (37) and determines the degree to which banking and insurance services connected therewith shall be liberalised. (38)

Title IV of Part Two deals with transport. The objectives of these provisions, which are to be supplemented by decisions of the Council, are to eliminate discrimination in national legislation relating to carriers by reason of the nationality of the carrier and to provide for a degree of uniformity in transport rates, including the extension of distance rebates over national frontiers within the

(35) Article 59. (36) Chapter 4 of Title II. (37) Article 52. (38) Article 61(2).
Community. In July, 1960 the Council adopted a directive prohibiting discrimination on account of the country of origin and destination of the goods. Extensive study of the problems in this field is being carried on by the Commission assisted by a consultative committee. Among other matters it is proposed to coordinate investment in transport.

Title I of Part Three of the Treaty deals with "Common Rules". Chapter 1 contains rules regarding monopolies, dumping and government subsidisation. Generally speaking subsidisation which distorts competition within the common market is not permitted. Chapter 2 concerns fiscal provisions. Internal taxes are not to be applied on products of other member states in excess of those applied to domestic products. There is to be some harmonisation of internal taxes levied in the various member states. Chapter 3 provides for the approximation of laws whose disparities cause distortion of competition in the common market.

Title II deals with economic policy. It provides for consultative machinery regarding economic trends and business cycles and on the overall balance of payments. If one member state is in serious difficulties the Council will look into the matter and may afford special assistance. This may consist of a concerted approach to other international bodies for assistance, the arrangement of limited credits by other member states and the authorisation of action to avoid trade diversion where the state in difficulties is restricting outside imports. During the transitional period special reductions in customs duties or enlargement
of quotas by other member states may be arranged in order to help the member state in difficulties. (39) Owing to the satisfactory balance of payments position of member states to date these provisions do not appear to have been used.

The final chapter in this Title concerns a common commercial policy. Article 113 provides that, after the expiry of the transitional period, the common commercial policy is to be based on uniform principles, particularly regarding tariff amendments, the conclusion of tariff or trade agreements, alignment of measures of liberalisation, export policy and protective commercial measures, including measures to be taken in the cases of dumping or subsidies. The Treaty requirements regarding movements of national tariffs towards the common tariff resulted, practically speaking, in an immediate loss of national autonomy in regard to tariff making and all tariff negotiation with outside countries has been carried on by the Commission. In July, 1962 the Council adopted a working programme for member states for a gradual introduction of a common commercial policy. Import restrictions are to be harmonised and full liberalisation is to be aimed at. This liberalisation will be first achieved for the European and dollar areas and later, when the problems of sensitive imports from low-cost countries is solved, it will be extended to all G.A.T.T. countries. There will be common quotas for communist countries. Export subsidies will be harmonised. Export restrictions will be abolished so far as is possible and so far as they remain Community quotas will be introduced. (39) Article 108.
The possibility of Community action to promote exports will be explored.

Title III deals with social policy. There must be equal pay as between men and women. (40) Under a decision of the Council this is to be fully achieved by the end of 1964. There is to be equivalence of paid holiday schemes (41) and of social security for migrant workers. (42) A European Social Fund is to ensure productive re-employment of workers by means of occupational retraining and resettlement allowances and to grant aid to workers in periods of unemployment due to conversion of their enterprise to other production. (43) This fund was set up in 1960 and was provided with fifteen hundred million Belgian francs for the remainder of the first stage.

The European Investment Bank is provided for in Title IV of Part Three. Its task is to grant loans and guarantees on a non profit making basis, to facilitate the financing of projects to develop less-developed regions, to convert large scale enterprises or create new activities and to finance projects of common interest to several member states. (44) Its funds are contributed by the members. It may also borrow from capital markets. A protocol annexed to the Treaty sets out the bank's statute.

Part Five of the Treaty concerns the institutions of the Community. The Assembly consists of members of parliaments of member states appointed by those parliaments. It is a deliberative body and meets at least once a year.

(40) Article 119. (41) Article 120. (42) Article 121.
(43) Article 125. (44) Article 130.
The Council is the governing body of the Community and is comprised of one ministerial delegate from each member state. For some purposes weighted voting is provided, otherwise each member has one vote. Abstentions by a member do not prevent the Council taking a decision requiring unanimity. The Commission is the executive body. On important matters it advises the Council and in other cases it exercises administrative powers. It is composed of nine members chosen for their general competence. The chairman of the Commission since its inception has been Dr Walther Hallstein of Germany. The Court of Justice is responsible for the observance of law and justice in the interpretation and application of the Treaty. (45) It is composed of seven judges. There is an Economic and Social Committee with consultative status. It is composed of 101 members chosen to represent categories of economic and social life. Title II of this Part deals with the Community's budget.

Part Six comprises "Final Provisions". These include the attribution of legal personality to the Community (46), provision for the fixing of the seat of the Community by common agreement (47), provision for negotiations regarding elimination of double taxation and the recognition of companies, judicial decisions and arbitral awards (48), provision for derogations from the provisions of the Treaty by a member state in case of serious economic difficulties (49); the preservation of rights and obligations under existing international conventions (50)

(45) Article 164. (46) Article 210. (47) Article 216 - the seat has in fact been established in Brussels but apparently without formal agreement. (48) Article 220. (49) Article 226 - limited safeguard measures have been authorised only in the case of Italy and Germany. (50) Article 234.
and provisions for new members or associations (51). The Treaty is concluded for an unlimited period. (52)

The Treaty, as can be seen from the above description, provides for a fairly high degree of economic integration, the exact extent of which has yet to be worked out and which may continue to increase after the end of the transitional period. It does not, however, provide for much surrender of sovereignty to a supra-national institution, not in fact so much as the Coal and Steel Treaty, nor does it provide for much financial integration though this has been recently proposed by the Commission. The governing body of the Community, the Council, being composed of ministerial representatives of each member state and sometimes requiring unanimity in its decisions, provides in such cases for preservation of the sovereignty of the member states.

(v) G.A.T.T. and the Rome Treaty

At the twelfth session of the G.A.T.T. in 1957 a committee was established to examine the Rome Treaty. The committee split up into four sub-groups which studied the following matters:

(A) Tariffs and Plar and Schedule; (B) Quantitative Restrictions; (C) Trade in Agricultural Products; (D) Association of Overseas Territories.

The last mentioned group was reconstituted as the Working Party on Association of Overseas Territories after the session and continued its work on into 1958.

(51) Articles 237 and 238. (52) Article 240.
The work of the G.A.T.T. in relation to the Rome Treaty has been a curious mixture of legalism, economic theory and concern about specific trade interests. By April, 1958 a deadlock had been reached on the legal issues and the Intersessional Committee in that month agreed that, at least for the time being, the Six would not be asked to do more than report to the G.A.T.T. sessions the steps being taken to implement the Treaty and to consult on request with one or more contracting parties in cases where the trade interests of these parties were threatened by the implementation of the Treaty.

The report adopted at the 1957 G.A.T.T. session expresses in relation to the common tariff the apprehensions of other G.A.T.T. countries that the tariff will be more restrictive than the individual tariffs and some criticism of the arithmetical average method of arriving at the common tariff and the replies of the Six on these points. (53) In regard to quantitative import restrictions the report summarises the divergent views of the Six and other contracting parties as to whether or not, according to the rules of the G.A.T.T., the Six are entitled to discriminate in favour of each other in the application of restrictions imposed for balance-of-payments reasons and whether they are entitled to maintain a common system of restrictions against third countries. (54)

Other members of the G.A.T.T. were on firm ground in their criticism of the agricultural provisions of the Treaty, such as minimum prices, long-term contracts and the common system of

stabilising imports and exports. They pointed out that these means did not make for free trade between the member states and that they appeared to raise barriers to trade with outside countries and implied the use of import restriction contrary to G.A.T.T. The main defence of the Six was that the policy had not yet been developed and that criticism ought to be stayed pending its determination. (55) In fact the policy as it has been worked out, although in principle of a trade-diverting kind, has avoided some of the technical breaches of G.A.T.T. that appeared inevitable by the development of ingenious tariff devices.

Criticisms levied by other member states against the provisions on the association of overseas territories included the fact that no complete plan or schedule had been laid down for the completion of the free trade area which the member states claimed would eventually be created between them and the associated territories and specifically that retention by the territories for an indefinite period of the power to levy duties on goods from member states for developmental and fiscal purposes rendered the arrangement no more than a preferential association. It was also noted that some of the territories were Trust territories and that under the United Nations Charter these could not give free entry to products of the Six without extending this to all countries. (56) This latter point is no longer relevant since the territories in question have become independent.

The report of the working party presented to the intersessional committee of G.A.T.T. in 1958 reflects the divergent views of the Six and of other members of the G.A.T.T. both as to the consistency of the association with G.A.T.T. rules and as its economic effects. The report contains sections on legal issues, economic issues, general issues related to the Rome Treaty, a summary of views of members of the working party other than the Six and commodity reports on cocoa, coffee, tea, bananas, sugar, tobacco, oilseeds, cotton, hard fibres, wood, aluminium and lead. (57)

In late 1958 and early 1959 consultations were held with the Six on the effects of the association of overseas territories and of the common tariff on trade in tobacco, cocoa, tea, coffee and bananas. The countries participating were Britain (on behalf of the colonial territories), Rhodesia and Nyasaland, India, Brazil, Indonesia, Canada, Dominican Republic, Turkey, Ceylon, Cuba, Ghana and the United States. In December, 1959 the Six held consultations at the request of Australia on lead, zinc and aluminium, other countries participating being Canada, Austria, Norway, Sweden, Ghana, South Africa and Britain.

The various moves in G.A.T.T. have probably had some influence on the Six in regard to their protective regime on tropical products and metals. The tariffs on metals that were subsequently fixed do not appear as protective as might have been expected whilst there are now moves afoot to replace preferences for the associated territories on tropical products by other means of assistance. It is too early to say how far this will be achieved but there have already been some reductions of a provisional nature in tariffs on these products by the Six.

The creation of a customs union will have economic effects both on the member countries and on the outside world. The breaking down of trade barriers will increase the trade between the member countries but will tend to diminish the trade between the member countries of the union and outside countries. The union will also tend to improve its terms of trade. However, if the net economic effect on the countries of the union is favourable, this will manifest itself in economic growth. This growth will in turn tend to increase trade with outside countries which, if the effects are large enough, may make up for their economic losses directly resulting from the formation of the union.

The picture may be set forth as follows — to me by Dr. W. K. Corden:

<table>
<thead>
<tr>
<th>Effect on countries of union</th>
<th>Effect on outside countries</th>
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</thead>
<tbody>
<tr>
<td>Favourable</td>
<td>Unfavourable</td>
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</table>

Trade creation, (specialisation, economies of scale).

Trade diversion,

(a) Direct trade effects
   Unfavourable
   Unfavourable

(b) Terms of trade.
   Favourable
   Unfavourable

Total of above

If favourable results in economic growth — Derived favourable effects.
Apart from the above effects, capital may be attracted into the union from outside sources and away from investment projects outside the union. This will have favourable effects on the countries of the union and unfavourable effects elsewhere. Resultant economic growth in the union may, however, have favourable effects on the trade of outside countries. There may also be offsetting effects if and when the union invests capital overseas.

(A) Trade Creation

The primary effect of trade creation in a customs union is ascribable to specialisation due to increased competition and to economies of scale. The latter may induce certain offsetting influences in the shape of monopolies restricting competition. Important to these effects is the mobility of labour and capital. The Rome Treaty shows an awareness of the importance of these secondary aspects.

Competition and economies of scale

The increase in welfare expected as result of the formation of a customs union is in great measure attributable to economies of scale. The greater division of labour rendered possible by the abolition of trade barriers and the creation of a larger market render possible the concentration of units of an industry in the most economical locations. This concentration may be either one involving the formation of large units or the aggregation of a number of individual units in one centre. In the latter case the economies are mostly external in nature and include both the geographical and other natural advantages of the sites and also
the derived economies due to the establishment of ancillary services. In the former case the economies are also related to the scale of the individual unit, the marginal costs of production of which are assumed to be smaller than average cost.

Where large units are established there is the possibility of monopoly practices becoming more serious. The assumption has, of course, already been made that there was some degree of imperfect competition in the smaller units but this should have disappeared when the optimum size was reached. The intensification of monopolistic practices arising from combination is likely to lead to a reduction of the increment of welfare anticipated through the decrease in average costs in the industry as a result of the increase in scale. The units are able to maintain abnormal profits and the consumer is denied part of the price reduction he could have expected due to the economy of scale.

Scitovsky (1) considers that European economic integration should lead to diminished protection of the small firm by governments thus leading to the replacement of such firms by larger and more efficient units. His reason for arriving at this conclusion is that small firms are almost always subsidised at the cost of and to the detriment of their larger and more efficient competitors and with free competition, few nations could afford to handicap their more viable enterprises in this or any other way. He points out, however, that the gains to be expected from international economic specialisation are not of a high order.

(2) This conclusion is reached from a fairly careful consideration

of the gains expected from specialisation. Moreover, the gain from increased specialisation among members is usually accompanied by a loss from decreased specialisation between members and non-members. (3) One important limit on the degree of specialisation likely within a union is that international cost relations need to be such as to avoid a pattern of reallocation that would raise the general level of activity in some and lower it in other countries. This requires a pattern of exchange rates that tends to minimise inter-country differences in money costs and leads to approximate equilibrium in each country's balance of payments. Under these conditions international specialisation follows the principle of comparative advantage and the extent of international reallocation is bound to be smaller than it would be if output were always concentrated in enterprises with the highest labour productivity. (4)

Another writer, Dell, (5) is even more sceptical regarding the benefits of expanding the market. He notes that it is freely asserted that American experience clearly demonstrates the advantages of a large integrated economy in exploiting to the full the benefits of mass production and specialisation but considers that the idea that the fullest exploitation of modern technology is obstructed by small national markets is not at all well documented. He considers that even the smaller western European countries have a national demand large enough to permit optimum

production of the great bulk of goods and services. In other cases they can obtain markets for surplus production by export. (6) He quotes a number of cases where a larger market has not led to superior productivity.

On the question of the size of the market, although this may not be so important or self-evident a factor leading to production economies as has been assumed by some writers, there will certainly be some cases, which Dell concedes, where a larger market is necessary to the establishment of industries of optimum size and without the necessity of exporting over the customs barriers of outside countries.

Professor Meade (7) has pointed out that it is not enough that the present size of the market provides scope for one plant of a sufficient size to enjoy all important economies of scale. To have a truly dynamic, competitive economy, a sufficiently large market is required to maintain a large number of competing plants of such a scale. (8) Sir Donald MacDougall takes the view that the present size of the British economy, together with its export markets, is adequate to make possible most economies of scale. The failure to exploit some of these economies through lack of standardisation could be remedied by measures other than entry into the Common Market (9).

In the European Economic Community, where factors of production are to be mobile, there is less reason to feel than in the case considered by Scitovsky that exchange rates will

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limit the extent of specialisation. Furthermore, there will be industries which have had only a small market and which have been highly protected, such as some of the synthetic fibre industries in the Six, which, under the impetus of the larger market are likely to expand considerably and in the process capture markets for competitive products.

Scitovsky has also pointed out that the freeing of European trade, by increasing the number and geographical coverage of the market outlets open to the average producer, would increase the number of firms he regards as his competitors. Although this could hardly lead to free competition, nevertheless competition will be less personal and therefore less considerate of the interests and profits of the weakest members of the group. National monopolies would probably be made less secure in their monopoly position, oligopolies are likely to be weakened; cartels, if extended from national into all-European organisations, are expected to come under the large and less under the influence of the small firms. This is likely to increase competition within the cartel organisation itself. The result should be to enhance the ability of the individual producer and his willingness and inducement to innovate and expand, by encroaching, if necessary, on the markets of his competitors. (10) Scitovsky holds the view that the gains from the spread of the more ambitious types of behaviour and the wider acceptance of the best industrial and commercial practices, from improved efficiency within individual enterprises and better allocation within individual countries, from lower profit margins (10) T. Scitovsky, Economies of Scale etc. page 89.
greater mass markets and from greater employment and price stability and the better utilisation of investment funds will be of a relatively high magnitude. (2) This contrasts with his view as to the benefits to be expected from specialisation. The importance of the "competitive jolt" is accepted by later writers such as Professor Meade and Sir Donald MacDougall.

Dell once again takes a pessimistic view and points out that there is no reason to suppose that restrictive business practices will not affect the degree to which competition will increase. In the case of the motor vehicle industry, which is most frequently cited as needing the stimulus of larger integrated markets to promote efficiency through greater competition and standardisation, there would be less difficulty than in most industries in maintaining restrictive agreements. (11) He is also doubtful as to the extent to which integration provides the most efficient means of spreading higher levels of productivity and per capita income throughout the territory. He points out that in France and southern Italy and in the United States the gap in economic development between regions has grown whilst employment in industry has been expanding faster in the more highly industrialised areas. (12)

The matters raised by Dell and Scitovsky are interesting in that they point to some of the many considerations that underlie the extent to which European economic integration will increase welfare. These points show the limitations to the formal

(11) S. Dell, op. cit. page 44. (12) S. Dell, op. cit. page 45
type of analysis put forward by Professor Meade in his earlier work, which will be discussed in the next chapter. This work analyses the effects of trade creation and trade diversion assuming a more or less mechanical system of competition. (12A)

On the matter of competition and restrictive practices it has already been the case that a large number of agreements have been concluded between industries and firms in the countries of the Community. Early in 1959 the Commission of the Community published a list of 245 of such agreements and the pages of journals since that time have reported many more cases. Such agreements are, in fact, as Dell suggests, important in the motor industry. (13) Expansion of trade and activity in the Community indicates that the agreements, whilst no doubt mitigating competition, have not entirely destroyed the fruits expected of competition. A G.A.T.T. publication, issued in 1962 (14), in commenting on the rate of expansion of trade between the Six, has stated that this had not brought out any clear evidence of significant shifts of localisation of industry inside the Community. However, this trade expansion had taken place in a period of rapid economic expansion. Moreover, where specialisation had developed, this tended to be concentrated on a range of particular products rather than on a branch of industry. Business agreements had also played an important part in this trade expansion.

The framers of the Rome Treaty were not unaware of the likelihood of economic polarisation and made arrangements for (12A) The limitations of his analysis are acknowledged by Professor Meade.

(13) The agreements reported by the Commission are industrial combinations rather than restrictive trade agreements.

special assistance to be given to relatively backward areas of the Community. Title IV of Part Three, establishing the European Investment Bank, provides for the use of the funds of the bank, inter alia, to finance projects for developing backward regions. (15) Whether the provisions of the Treaty will in operation prove adequate to meet the problem remains to be seen.

The Treaty, as has been noted, also contains provisions regarding competition, which are set out in Chapter 1, Title I of Part three. These rules not only cover such matters as dumping and aid to industries by states but also regarding restrictive practices.

The parties to the Rome Treaty were neither blind to the need to ensure that competition within the Community was not stultified by the growth of monopoly powers nor did they ignore the fact that some degree of business concentration among firms

(15) Article 130 (a).
in different countries of the Community would ease the process of integration. Therefore whilst the Rome Treaty commences the relevant chapter by declaring that agreements between enterprises which are likely to affect trade between the member states and which have as their object or result the prevention, restriction or distortion of competition within the common market, are incompatible therewith, are prohibited and are null and void between the parties, it quickly goes on to give the Commission, within the framework of directives by the Council, power to declare these provisions inapplicable in individual cases. These cases are the ones which contribute to the improvement of the production or distribution of goods or to the promotion of technical or economic progress, while reserving to users an equitable share in the profit resulting therefrom. Moreover the cases in question should neither impose on the enterprises concerned any restrictions not indispensable to the attainment of the objectives nor enable such enterprises to eliminate competition in respect of a substantial proportion of the goods concerned. (16)

Certain monopoly practices by enterprises having a dominant position in the Community are, however, without exception prohibited. These consist in the imposition of

(16) Article 85.
inequitable purchase or selling prices or other inequitable trading conditions; the limitation of production, markets or technical development to the prejudice of consumers; the application to parties to transactions of unequal terms in respect of equivalent supplies, thereby placing them at a competitive disadvantage; or the subjecting of the conclusion of a contract to the acceptance by a party of additional supplies which, either by their nature or according to a commercial usage, have no connection with the subject of such contract. (17) As in the case of agreements, the enforcement of these provisions is left to the Commission under directives (18) by the Council. Fines and penalties may be imposed for breach of the provisions in both cases. (19) Member states are required to follow the same rules in regard to state trading enterprises. (20) The Council had three years in which to establish its rules, that is until the end of 1960 and in the intervening period the enforcement of these provisions was left to the authorities of the member states. (21) The Council has in fact now established rules.

**Mobility of labour and capital**

The Rome Treaty provides for the abolition within the transitional period of restrictions on the movement of workers. Workers are to be free to move from one country to another to

(17) Article 86. (18) Articles 87, 89. (19) Article 87(2)(a) (20) Article 90. (21) Articles 87, 88.
take up actual offers of employment, to stay in the new country while employed and thereafter, subject to conditions to be laid down. (22) The worker can also remain in the new country to carry on a non-wage earning activity provided he fulfils the conditions which would have been necessary if he had in the first place moved in order to establish such activity. (23) Such mobility will be assisted by some measure of integration of social service schemes. (24)

Apart from occupational mobility between member states, the Treaty also contains provisions requiring equal pay for men and women the equivalence of paid holiday schemes and regarding the retraining of workers with the aid of the Social Fund. (25)

It is difficult to predict the effect of these provisions on the economy of the Community. Whilst provisions regarding equivalence of working conditions will no doubt lead to a levelling upwards of the standard of living of workers, notably of the German worker, towards the level of advantages enjoyed by his French contemporary (26), and thus have some inflationary influence on the economy, the provisions for mobility of labour should have noticeable effects on the elimination of waste through unemployment. This is particularly important in a time like the present when the economy of the

(22) Article 48 (23) Article 54 (3) (d). (24) Articles 118, 121. (25) Articles 119, 120, 215. (26) These advantages are in the social benefit and leisure fields rather than in relative real wages.
Community is expanding and labour shortages are common.

The question must be raised whether the labour mobility provisions coupled with the provisions on establishment, will not lead to further concentrations of industry in areas like the Ruhr and further depletion of economic activity in the relatively backward areas such as southern Italy and central France. The provisions of the Treaty for restraining such centralisation, such as the creation of the European Investment Bank (14), are hardly strong enough to withstand such movements. If any great shifts occur from one country to another, this may have unfortunate political effects as the first country will resent its loss of economic strength. The American experience does not suggest that the dis-economies of centralisation beyond a certain point are likely in themselves to restrain a movement which is greater than desirable. One weapon that the member states of the Community may use during the transitional period, with the permission of the Commission, is protective measures against dumping. (27) However, this privilege will disappear after the transitional period when reliance will need to be placed on the rules prohibiting unfair business practices. Dumping is an important factor in restraining the maintenance and growth of industries in relatively backward areas where the distance away from the industrial area is sufficiently great to effectively stop the

(27) Article 91.
re-export of the product to the industrial area. Such practices appear to have been instrumental in retarding industrial development in parts of the United States and Australia. The effectiveness of the instruments devised to combat this in the Community will need to be proved.

Mobility of the labour force within a customs union is desirable because it renders more feasible the equalisation of remuneration and conditions of employment of workers in the various member states. This greatly facilitates freedom of competition. In the absence of equivalence of labour costs, German industry with its relatively low cost structure would continue to dominate French industry with relatively high labour costs and there would be a perpetual payments problem between the two countries. There might eventually be some alleviation of the position through the growth of the power of organised labour in Germany but this would be a slow and painful method of harmonising conditions and an uncertain one. Mobility of labour combined with conscious efforts to harmonise remuneration and working conditions will accomplish the equalisation of labour costs more swiftly and surely. (28)

The question of mobility of factors such as labour and capital has been studied by a number of writers whose conclusions have been summarised by Sannwald and Stohler. (29)

(28) Some harmonisation appears to have taken place within the Community for other reasons than labour mobility, e.g. exchange adjustment (29) Sannwald and Stöhler, Economic Integration (1959) Chapter VI.
Whereas Ohlin pointed out that mobility of goods to some extent compensates for the lack of inter-regional mobility of factors (30), Samuelson, working with a model of two freely traded commodities, concludes that, except when the factor endowment in the countries differs too greatly, commodity mobility is a perfect substitute for factor mobility (31). In this model transport costs are neglected and, in taking account of these costs, a measure of factor mobility may become desirable. It is also noteworthy that an assumption is made in each case of decreasing marginal productivity.

Sannwald and Stohler point out that migration of labour is not entirely without cost and that this cost must be set off against the gains otherwise accruing thereby. Furthermore, they point out that it is desirable to harmonise social legislation, as differing social legislation may cause migration of skilled workers away from poorer countries where social security charges are higher. (32) The Rome Treaty does indeed take account of the need for harmonisation of social charges and benefits.

B. Trade Diversion

Trade diversion is an inevitable consequence of the formation of a customs union. If France formerly imported a
product from England at a price 5 percent less than it was obtainable from Germany and France enters into a customs union with Germany, an external tariff of, say, 10 percent will induce French importers to buy the product from Germany in preference to England. This "trade diversion" although benefiting Germany, appears to cause an overall loss of economic welfare as the products of the less efficient producers are now being bought in preference to those of the more efficient producers. The degree of trade diversion will be greater, the higher the level of the common tariff and other barriers to importation into the customs union. This is why there has been much concern about the level of the common tariff of the Community and the extent of other barriers to trade and why the G.A.T.T. lays down rules regarding customs unions which attempt to ensure that these barriers are not increased over the level of those existing previously in the constituent countries.

There are considerable opportunities for diversion of trade in primary products as a result of the formation of the European Economic Community which occasion concern to countries exporting these products to the Six. In this connection it is relevant to note that a high degree of protection for the production of foodstuffs had developed in Europe prior to integration and also in other industrialised countries, notably the United States.

This had already had certain trade effects. Numerous
studies by the G.A.T.T. had shown a tendency in the post-war period for the trade of industrialised countries to increase at a more rapid rate than that of primary producing countries. A leading authority remarked that prosperity of the industrialised countries was a necessary but not a sufficient condition for growth in the primary producing countries. (33).

The matter was discussed at some length by a committee presided over by Professor Haberler, which ascribed this state of affairs largely to the trade policies followed by industrialised countries. The terms of reference of the committee dealt particularly with agriculture and the question of the highly protective policies followed by the industrialised countries in the agricultural sector was developed at some length in the Committee's report. (34) The Committee did, however, also find it necessary to point out that the industrialised countries also followed restrictive policies against cheap manufactured goods from countries in the early stage of industrial development. The conclusion is therefore that the economic development of developing countries is being retarded in many directions by the unwillingness of industrialised countries to import.

These considerations are important in arriving at conclusions as to the likely economic effects of the

creation of the Community. It might be expected that the increased prosperity of the area would lead to an increased demand for imports as is in fact likely to be the case. Nevertheless the question whether the primary producing countries and less-developed areas will stand to benefit depends on the specific policies followed by the Community on the import of agricultural products, raw materials and the types of manufactured goods exported by developing countries.

The import policies of industrial countries in regard to these products is largely conditioned by the fear of disruption to domestic production where such production exists. The high degree of price fluctuation in the field of primary commodities, particularly foodstuffs, has led to the creation of highly protected systems where tariffs are supplemented by variable fees and import restrictions, in order to protect the income of farmers and other primary producers. The low price of manufactured goods from less-developed countries has equally led to restrictive measures limiting the quantity of such goods admitted into industrialised countries.

The Haberler Committee, without concerning itself unduly about methods of protection, though it expressed a preference for deficiency payments to other methods, has urged that there be some measure of reduction in the level of protection of agriculture by the industrialised countries.
Quite a moderate reduction in this level would significantly increase the demand for agricultural imports. Industrial countries, least of all those of the European Economic Community have not shown themselves willing to face the political difficulties of planning for an overall reduction in the level of protection and consequently of the level of production of specific agricultural commodities. They have been fortified in this policy by the knowledge that most of the world is hungry and that serious food shortages are anticipated later in the century. Any solution to the problems of agricultural trade is therefore unlikely to demand curtailment of production by the industrialised countries.

In the industrialised sphere there is reason to expect that the trade-diverting effects of the creation of the Community will be more than offset by the trade-creating effects of economic growth and prosperity. The increase in demand for imports of industrial goods by countries in the process of development is a well-known phenomenon. It is true that difficult problems exist in regard to the increase of imports of industrial goods from developing countries because of the disruptive effects of low-priced goods upon internal markets. These goods include not only cheap cotton textiles and clothing from India (Japan is not classed as a less-developed country) and Hong Kong
but also a variety of industrial goods such as bicycles, table lamps, small diesel engines, electric fans, sewing machines and sporting goods from Brazil, India, Pakistan, Hong Kong and other industrially developing areas. Nevertheless international feeling on this issue is so strong that there is reason to hope that the Community will find ways and means to increase its intake of these cheap industrial goods. The Economic Commission for Europe has suggested that the conditions necessary for the requisite imports of industrial goods from less-developed countries into Europe are an adequate overall rate of growth in Europe and the necessary adjustments in the domestic industrial structure of western European countries to be undertaken in time to avoid absolute declines in any major industry, thus provoking recourse to protective measures. (35) That it is practicable for the Six to increase imports from less-developed countries even in the face of such an industrial decline is, however, indicated by the agreement of the Six, in the context of the G.A.T.T. Cotton Textiles arrangements, to increase import quotas for these textiles. This arrangement also contains safeguards against violent

disruption of markets by imports.

One study of the likely development of policy in regard to production and imports of the Six reaches the following tentative conclusions in regard to foodstuffs:

Foodstuffs (thousand million dollars at 1953-55 prices)

<table>
<thead>
<tr>
<th></th>
<th>1953-55</th>
<th>1973-75 (prospective)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value of production</td>
<td>16.15</td>
<td>26.25</td>
</tr>
<tr>
<td>Net imports:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Coffee, Tea, Cocoa,</td>
<td>0.65</td>
<td>1.00</td>
</tr>
<tr>
<td>Other foodstuffs.</td>
<td>1.35</td>
<td>0.00 (36)</td>
</tr>
</tbody>
</table>

The same study gives the following figures on imports of raw materials:

Raw Materials (thousand million dollars at 1953-55 prices)

<table>
<thead>
<tr>
<th></th>
<th>1953-55</th>
<th>1973-75 (prospective)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fuels,</td>
<td>0.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Ores and metals,</td>
<td>0.5</td>
<td>1.25</td>
</tr>
<tr>
<td>Natural textile fibres,</td>
<td>1.3</td>
<td>1.25</td>
</tr>
<tr>
<td>Natural rubber,</td>
<td>0.2</td>
<td>0.3</td>
</tr>
<tr>
<td>Wood and pulp,</td>
<td>0.6</td>
<td>1.0</td>
</tr>
<tr>
<td>Other materials.</td>
<td>0.3</td>
<td>0.55 (37)</td>
</tr>
</tbody>
</table>

These figures are not heartening to the agricultural exporting countries. They do not appear unfavourable to the producers of tropical goods but any benefit to this group is likely to be taken up by the countries associated

(36) The possible impact of the European Economic Community, particularly the common market, upon world trade, (G.A.T.T.), December, 1957, page 32.
with the Community rather than the less-developed countries in general.

The G.A.T.T. study does not give any detailed analysis of trade diversion but is concerned more with the effects on imports of variations in the increase of Gross National Product and the decrease of the agricultural labour force. Although the above figures are those most frequently quoted in the study, alternative estimates for 1973-75 are made using different assumptions. These are discussed below.

The following is a simplified illustration of sectoral growth with and without union:

<table>
<thead>
<tr>
<th>Units, at constant prices.</th>
<th>With union</th>
<th>Without union</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Industry</td>
<td>Agriculture</td>
</tr>
<tr>
<td><strong>Production</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Initial</td>
<td>300</td>
<td>200</td>
</tr>
<tr>
<td>Ten years later</td>
<td>450</td>
<td>275</td>
</tr>
<tr>
<td><strong>Import requirements</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>from outside countries</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Initial</td>
<td>120</td>
<td>80</td>
</tr>
<tr>
<td>Ten years later</td>
<td>275</td>
<td>75</td>
</tr>
</tbody>
</table>

This illustration assumes, in the case of union, utilisation of the whole of the increase in national product in the approximate proportions of seventy percent industrial and thirty percent agricultural and in the case of absence of union thirty six percent agricultural and sixty four percent
industrial.

The extent of trade diversion is concealed in the figures but it is apparent that in the case of agriculture diversionary effects exceed trade-creating effects by fifteen units whereas in the case of industrial goods trade-creating effects exceed diversionary effects by sixty-five units. It is not possible to separate the two effects as the increase of income is to a large extent ascribable to trade diversion arising from the creation of the common market. It is unreal to compare the position with a notional increase assuming no external barriers as the absence of external barriers might be disastrous for the union.

The above illustration holds good for a determined level of production increase arising from union. However, depending on the features of the union, national income and production may grow to a greater or lesser amount. The G.A.T.T. study (38) assumes varying rates of increase of Gross National Product. In the estimates of imports, the import of manufactures varies considerably with the growth in G.N.P. The import of foodstuffs, however, is shown as varying inversely with the growth in G.N.P. but in the same

direction as the decline in the agricultural labour force. As these two factors are likely to work together, that is, the larger the growth of GNP, the larger is likely to be the decline in the agricultural force, the estimated effect on agricultural imports of variation in levels of G.N.P. is unpredictable. The reason given for the primary effect of accelerated growth of G.N.P. being adverse to agricultural imports is that agricultural productivity per person would need to increase greatly to keep pace with growth of industrial productivity. Governments, moreover, would be concerned to see that the relative position of agricultural incomes did not deteriorate. The rise in production would be greater than the increase in demand for food. (39)

The extent to which the heavy increase of foodstuffs production in the Six denotes an increase or decrease in welfare generally speaking depends on the degree to which the efficiency of agricultural production in the Six can be increased. There is undoubtedly great scope for increase of efficiency in the Community's agriculture, especially through the consolidation of holdings, but it is likely that this increase will be carried through if need be under the umbrella of highly protective measures. In this case the effect on welfare generally of the world may be negative.

This appears to be the case with American agriculture which, not only in foodstuffs production but also in the production of raw materials like cotton and wool is highly protected. This protection may, indeed, by afforded at the expense of the industrialised sector, which is so prosperous that the burden is hardly noticed internally but it is noticed by other countries, whose opportunities to supply foodstuffs and agricultural raw materials to the American market have been reduced to negligible proportions and who have to suffer restriction of their markets elsewhere to make room for subsidised exports of American produce. (40). All these problems became apparent in relation to the Six, well before the formation of the Community.

At this stage it can be said that the problems are likely to be intensified as regards outside countries, the higher are the external barriers to trade with the Six and the higher as a consequence the trade-diverting production induced within the Community. On the other hand

(40) There are a number of anomalies in the situation which were not adequately dealt with in the Haberler Report. In the case of America it may be argued that the protective policy enables the utilisation of land resources to produce food for starving peoples. The anomaly appears to come about because of immigration restrictions which keep living standards so high that wages are at a level making agriculture uneconomic. Another contention, relevant to the Community, is that it is only under the umbrella of protection that adequate structural improvement will be made to agriculture so as to facilitate its increased efficiency.
they are likely to be lower the more genuine is the freedom of trade within the Community, with consequent elimination of inefficient production. In this connection, the term "freedom of trade" is somewhat wide, as if all Community producers are assured a high uniform price for their production of a commodity, this will tend to maintain inefficient production in the same way as internal barriers would do, except that the total level of Community production would be higher.

In the specific case of the Community, the external tariffs on foodstuffs are on the high side and their protective effect will be reinforced by variable levies and in emergencies by import restrictions. The Six are virtually self-sufficient in wheat and dairy products and appear to be aiming at greater self-sufficiency in coarse grains. Sugar and meat are other products where there is a possibility of fostering internal rather than external trade. Variable import levies will operate in much the same way as import restrictions. They will be fixed at a level to assure the disposal of all domestic production internally insofar as it is not actually in surplus to domestic consumption requirements. The signs are that greatly expanded production of foodstuffs will be undertaken in the Six, notably in France. This is revealed in the Franco/German grain agreement and in French official agricultural plans.
Moreover, there is as yet no sign that relatively inefficient Italian dairy production is to be discontinued in favour of efficient Dutch production or that relatively inefficient German or Italian grains production is to be sacrificed to more efficient French grains production. The decisions taken so far are in favour of prices sufficiently high to keep in being existing relatively inefficient branches of agriculture. Nevertheless, there will be time over the ensuing years to vary this policy. The American example is, however, not encouraging.

A leading authority, in discussing customs unions, has remarked "the economic case for removal of trade barriers loses some of its logic when the setting is not that of one where prices and money cost of production are determined by the free play of demand and supply in competitive markets." (41) "Economic planning has made trade barriers protective of more than the allocation of resources and has thus made their removal a much more delicate and economically debatable matter. (42)

These matters are all of considerable importance in regard to the Community, particularly in the agricultural sector. Principles of free competition in this sector are not prevalent in the Six and it will require great efforts, perhaps too great, to develop it among the countries concerned.

(41) Jacob Viner, The Customs Union Issue, 1950, page 137.  
(42) Jacob Viner, op. cit., page 138.
The harmonisation of agriculture in Benelux planned to be accomplished by 1962, still leaves much to be achieved sine die. The problems presented in the wider framework of the Six are very much more difficult though they are being tackled. Economic planning is not confined to the agricultural sector but is very important there as deliberate policies to place the income of the farmer on some sort of parity with his fellows in other occupations are widely followed. The caution with which agriculture has been treated in the framework of the Rome Treaty reflects a desire to maintain this objective.

It may be noted that, as the common agricultural policy has been developed at present, it appears to rest almost entirely on a price mechanism. The assumption has been made throughout the discussion in this chapter that higher prices will lead to higher production. Although this is certainly not always the case where farmers are operating at subsistence levels of income, it appears reasonable in the circumstances likely to prevail in the Community.
The European Economic Community

Chapter 4.

(b) Economic Consequences

Economic changes

It is apparent from the previous chapter that trade creation and trade diversion bring about a number of economic changes such as economic growth and changes in welfare. The present chapter must be regarded as a continuation of the discussion which is separated for convenience rather than logically from that which has been initiated in the foregoing chapter.

Changes in welfare

Under this heading it is intended to look at a series of propositions put forward by Professor Meade (1) which examine from the point of view of changes in welfare the economic effects of the creation of a customs union and to consider the application of these propositions to the European Economic Community. Meade's proposals, however, do not deal adequately with the relative spread of any economic gain as between members of the union and outside countries, which is of particular interest in regard to the problems under study.

Treating the subject empirically, it may be postulated that the less severe the barriers to trade with outside countries, the more likely are benefits to accrue to them. Though little if any benefit in the case of the Six may flow to exporters of temperate agricultural products, considerable benefit may accrue to exporters of industrial

(1) J.E. Meade, Notes on the theory of customs unions, (1955). These propositions are here cited as being of Meade. Some, however, are derived from the earlier work of Viner (The Customs Union Issue (1950)) and the propositions are repeated virtually unchanged in Sannwald and Stohler, Economic Integration, (1959).
goods. However, one particular feature of the Community indicates that some delay will occur before outside exporters of industrial goods will experience much benefit. This is because of the exceptional industrial strength of Germany which will tend to divert trade of other members of the Six away from outside countries. As living standards in Germany improve, this position should moderate and there are signs that such moderation is under way. It might be expected that this internal concentration of benefit in the early stages will be made manifest by improvement in the terms of trade of the Community with outside countries.

The first proposition of Meade is that the formation of a customs union is more likely to lead to a net increase in economic welfare if the economies of the partner countries are actually very competitive or similar but potentially very complementary or dissimilar. (2) This he links to his third proposition that such net increase is also the more likely to occur the higher the initial rates of duty between the partners. (3) In the case envisaged by him the partners A and B are each producing products X and Y; A produces X efficiently, B, Y; A's initial duties are high on Y, B's high on X; after integration A will specialise on its efficient lines of production in accordance with the classic theory of international trade. It is noteworthy that it appears to be differences in the external duties of A and B rather than

their absolute levels that appears to be relevant.

Meade's second proposition merely points to the fact that the formation of a customs union is likely to lead to some primary expansion of trade leading to economic gain but that this may be offset by secondary effects. (4) He considers that the gain is the more likely if each partner is the principal market for the products of the others as there will be less diversion of the trade of outside countries. (5) His fifth proposition is that the likelihood of economic gain is the greater, the larger the proportion of world trade, production and consumption covered by the union as there is also in this case less scope for trade diversion from the rest of the world. (6) It may be remarked, however, that outside countries are in practice sceptical of the effects that too powerful economic blocs have on their welfare. There may be indeed less trade diversion in the world as a whole in the case of a large union because the number of countries included in the union and therefore not suffering trade diversion is larger but the trade diversion suffered by those left outside may be more intense.

Another proposition is that gain will be likely to be greater the lower the rate of import duties in the rest of the world but the greater the number of independent customs areas into which the rest of the world is divided. (7)

(7) J.E.Meade, op.cit., pages 109/110.
This is propounded in relation to relatively cheap exports of a partner to an outside country. The formation of the union may lead to diversion of these exports to another partner but the former customer may be able to buy elsewhere if a sufficient number of countries exist. This proposition is interesting in bringing out a further form of diversion that may occur though the analysis of final effects appears to be somewhat incomplete. A further proposition indicating circumstances in which diversion is minimised is where the original barriers between all partners are quantitative. In such a case there will, according to Meade, be normally no secondary trade diversion. Even where the arrangements with outside countries do lead to such diversion, he considers that there will be no less of economic welfare. This is the case where trade with outside countries was formerly free and trade with partner countries was not. This theory may have played a part in the development of the O.E.E.C. trade liberalisation programme.

His final propositions are that economic gain will be the greater, the greater the scope for economies of scale, and that partial reductions in duties between the partners are more likely to be beneficial than the final steps towards abolition. In view of the strong views that are held within the G.A.T.T. on the undesirability of preferential associations and the acceptability of complete customs unions,

(8) J.E. Meade, op. cit., page 110.
(9) J.E. Meade, op. cit., pages 110/1. Economies of scale were discussed in the preceding chapter.
this proposition appears to be surprising. G.A.T.T. works on the assumption that it is the final stages of removal of duties that really hurts and that it is as a result of these final stages that competition becomes intensified and resources become reallocated. The question whether G.A.T.T. is carried away by dogma or whether Meade's proposition is fallacious is an important one and will be further considered. Two cases will be set out where Meade's proposition does not appear to apply and this will be followed by discussion of the general theoretical position.

It is first necessary to note the importance of the stage in reduction of duties when competition becomes important between members of the union. In the following set of circumstances a partial reduction of duties can only lead to diversion of trade and not to any overall increase in welfare. Suppose product X is produced in A at one cost and that the cost in B is 5 per cent cheaper and in C 15 per cent cheaper than in A and that there are no cost variations over the range of production under consideration. A has a tariff of 15 per cent, B one of 10 per cent on the product. A and B form a customs union. Within the union A and B reduce their tariffs on the product to 5 per cent and nil respectively. There will as a result be no increase in competition as A's industry will be adequately protected against that of B. On the other hand any import trade of A may be diverted from C to B as B now has a 10 per cent preference in the market of A over C and is competitive in that market with C. If that
occurs A's economy appears to have suffered some loss as it is in effect paying 10 per cent more for the product, this difference being reflected in decreased collection of import duties. Moreover B's gain is offset by C's loss.

In the following case changes in welfare may be small in the early stages of tariff reduction but large later on. This case is relevant to the Community. As the economies of the Six are relatively similar, the assumption may be made that many duties on each other's goods are higher than protective considerations justify. The tariffs may be set at their current height because of competition from the United States or Japan. If this is the case partial reductions of duties may have little effect on competition between the Six; the case noted above. It is not until duties have been reduced to the point where the product of the partner countries competes with domestic production that the welfare effects to be discussed below come into play. From that point the domestic industry must either reduce its profits or its cost or disappear. In the case of some products such as motor cars there may be a special market for the imported product based on a consumer desire for product differentiation. In such a case tariff reductions will create trade in favour of the partner country at a stage before the imported product competes with the local product. But this trade creation is likely to be at the expense of imports from outside countries and so therefore offset, in global welfare terms, by trade diversion.
Looking at the problem from the more general theoretical viewpoint, it may be noted that Meade is treating the matter on a partial basis. He is isolating individual effects, assuming all other matters are normal. He is working on the normally shaped supply and demand curves on which it is easy to demonstrate that consumer surplus will increase at a diminishing rate as tariffs are reduced. It is likely that the supply curve of other members of the union is more elastic than that representing supplies from the member whose market is being considered and this is a normal assumption in the consumer surplus diagram. But what may well happen is that the supply curve of domestic production is highly inelastic in the early stages of tariff reduction but becomes highly elastic in later stages. Here there is a potentiality of greater "trade creation" in the later stages of tariff reduction than in the earlier.

But even in such circumstances it is not apparent that increases in welfare will be greater in the final stages of tariff elimination. Suppose a case where a tariff of 15% is being eliminated and that the supply curve of domestic production is inelastic over the first 10% of reduction but very elastic thereafter. In the early stages of tariff reduction the increases in welfare are due to the improved "consumer choice" available through the diminution in price in the article and the decrease in "excess profits" of the producers in the domestic market. In the final stages of tariff reduction the benefits to "consumer choice" will continue
and, as in the normal case noted above, these benefits will be of diminishing value. But there will also occur the disappearance of the domestic industry and the creation of increased import trade from the partners of the union. As this will involve capital losses in the importing country and capital expenditure in the exporting partners, the particular economic value of this "trade creation" is not immediately apparent. The G.A.T.T. proposition is thus seen to rest on the assumption that the disappearance of the industry in the importing country and its expansion elsewhere in the union will be accompanied by cost reductions due to specialisation and economies of scale as the small initial cost differences in the case just considered would not in themselves make the "trade creation" that has occurred particularly valuable.

The fact, however, that a rationale has been found for the G.A.T.T. proposition by no means establishes the G.A.T.T. contention as a valid one and that of Professor Meade as an invalid one. In the previous chapter it has been noted that writers such as Scitovsky consider the gains likely to result from specialisation and economies of scale in the Community as being of a rather low order but the gains from increased competition as likely to be fairly high. As the former gains are those accruing from the final stages of tariff reduction and the latter those resulting from the initial stages, the final conclusion is that Professor Meade is not altogether wrong.
However, from a more general point of view it appears that if a group of countries are in an economic union, there seems little merit in the maintenance of small residual barriers to trade, such as low tariffs, to preserve existing industries. Some excuse might be found for such barriers in order to solve employment, budgetary and balance of payments problems of the individual countries in the union. But if the aim of a union, such as the Community, is to place these problems on to a group basis, there is no virtue in internal barriers on a national basis. National boundaries are purely fortuitous and if there were any virtue in internal barriers at all this would rather be on a geographical basis, say in mountain valleys which might otherwise become depopulated.

To sum up Professor Meade's propositions in their relation to the Community, it appears that the Community appears to measure up fairly well to Meade's criteria for beneficial effects, looking at the matter generally and confining attention to the industrial sphere as so much remains in doubt as to the course of integration in the agricultural sector. The economies appear to be competitive and potentially complementary. There are fairly high duties on each other's goods and these vary considerably in incidence as between the Six. Other countries are numerous, many have relatively low duties and alternative sources of supply are available. The area covers a relatively large segment of world trade between countries of the area before integration.
On the other hand, it will be seen that the opportunities for economies of scale may not be large (though this is a matter on which a variety of opinions exist) and it is also a fact that most quantitative barriers had been abolished before integration.

The general conclusion is that the formation of the Community should lead to a general increase in welfare so far as industrial integration is concerned. The position may be otherwise in the agricultural sector though the overall effects are not likely to outweigh the favourable industrial effects. The welfare of countries exporting agricultural products to the Six may, however, be adversely affected. Many of these countries are in fact seeking association of the Six. Such a solution is not, however, so obviously practicable for many countries exporting to Britain, if the Community is expanded to cover Britain.

**Economic Growth**

As a complement to the trade-diverting effects of the formation of the Community, consideration must be given to factors related to economic union which tend to create growth. It is not possible to determine from the available evidence whether or not the formation of the Community has tended to maintain growth that otherwise would have declined (10); in view of the low rate of growth in Britain there is,

however, reason to feel that this may have been the case.

The following are some figures illustrating growth rates:

<table>
<thead>
<tr>
<th>Country</th>
<th>Increase of G.N.P. per annum</th>
<th>Per cent per man employed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1950-55</td>
<td>1955-60</td>
</tr>
<tr>
<td>Belgium</td>
<td>2.7</td>
<td>2.2</td>
</tr>
<tr>
<td>France</td>
<td>4.0</td>
<td>3.4</td>
</tr>
<tr>
<td>Germany</td>
<td>5.7</td>
<td>4.0</td>
</tr>
<tr>
<td>Italy</td>
<td>4.8</td>
<td>3.5</td>
</tr>
<tr>
<td>Luxemburg</td>
<td>0.9</td>
<td>2.6</td>
</tr>
<tr>
<td>Netherlands</td>
<td>4.2</td>
<td>3.0</td>
</tr>
<tr>
<td>Britain</td>
<td>2.1</td>
<td>2.1</td>
</tr>
</tbody>
</table>

The above figures show that, except in the case of Luxemburg, there has been a decline in growth rates of recent years in the Six. Such a decline could be expected as the high rate of growth in the early 1950's represented a catching up of arrears caused by the war. Only part of the latter period represented one in which the Community existed, though E.C.E.C. covered this period. Suggestive of integration is the rapprochement of growth rates in the Six; in the earlier period these varied from 0.9 to 5.7 per cent, in the later period from 2.2 to 4.0 per cent. In July, 1962 the Commission reported that gross product of the Community was some 20 per cent by volume above that of 1957 and that growth had been more balanced than in the past. (12) Indicators quoted for 1961 (1957=100) were G.N.P.(volume) 121; Industrial production

Recent figures show that growth in the Community is continuing at relatively high levels.

If it is tentatively concluded that maintenance of growth is linked to integration it is worth while examining some of the causes that could make for such growth. The relation between certain factors and growth was assumed in the diagram set out at the beginning of Chapter 3.

One possible cause of growth is an increase of profits available from trade within the Community due to the larger market resulting from abolition of trade barriers. This is allied to trade-diverting effects affecting growth adversely. Another aspect of the creation of the larger market, not offset by trade-diverting effects, is the increase of efficiency due to increased competition and the possibilities of large-scale production; these have already been discussed at some length.

Whilst the formation of the Community may, at least in the early stages not lead to the effects mentioned above, it has occasioned a degree of confidence which has tended to promote economic growth. Firms have planned for a larger market, often in conjunction with firms elsewhere in the Community and have reorganised their production and marketing facilities. This has led to considerable new investment. This investment has been partly with funds

(13) E.E.C. Commission, op. cit., page 47.
attracted from outside the Community, from Britain and the United States, whose investors have seen the possibility of good profits in the larger market. Secondly, there may have been a more efficient employment of capital already within the Community. This would include not only capital tempted from dormancy by the offer of higher returns but also the fuller utilisation of under-employed resources and more efficient investment of capital. Funds that formerly would have been invested in small-scale, relatively inefficient plants may now be invested in larger, more efficient plants. These changes may involve an increase of capital per worker and should in any case involve increased productivity of the combination of capital and worker; because there will also be fuller utilisation of the labour force. The economic surveys produced by the Community show that the labour force has in fact become the factor limiting economic growth in the Community. In the absence of integration bottlenecks of a different kind may have developed.

The dilemma confronting developed countries is that rapid economic growth will not take place unless an adequate pressure of demand on productive resources is maintained. Determined governmental action can promote rapid growth for a period even when the external position is weak. But re-establishment of the country's world competitive position will be necessary in such cases if successful growth is to continue. (11) Weak export demand has more generally been due to relationship between growth and price stability - the
faater is the rate of increase of output and productivity, the easier it is to prevent costs from rising. (11)

It appears that in recent years Britain has not been able to solve this dilemma but that the problem has been less acute for the Six. The German economy had at least for several years solved the problem of growth by reason of technical efficiency and by discipline that ensured that a great deal of the resources produced by export profits were ploughed back into capital development rather than used in increased consumption. In France there was a lack of discipline and the effect of devaluations was soon spent in renewed inflation. This discipline was, however, eventually introduced under the stronger government of de Gaulle and the last devaluation was accompanied by effective restraints on costs and the economy benefited from a greater degree of planning. It appears probable that the success of French reorganisation would have been assisted by economic integration measures under the Rome Treaty. Such matters as the Franco/German Grains agreement and the German and Dutch revaluation would have assisted France's external position.

Terms of Trade

Viner has pointed out that the formation of a customs union may lead to an improvement in its terms of trade to the disadvantage of the outside world. This is because "the greater the economic area of the tariff unit, other things being equal, the greater is likely to be the elasticity of
its reciprocal demand for outside products and consequently the greater the possibility of improvement in its terms of trade through manipulation of its tariffs." (14) Viner also points out that the larger bargaining unit has greater power to induce other countries to reduce their tariffs. (15) He points to a number of cases where closer union was sought to improve bargaining power and he also put forward a case to show that early movements for European economic integration were inspired by a desire to stand up more effectively to American practices and competition.(16).

It seems fortunate that the General Agreement on Tariffs and Trade, with its rules on customs unions, was in force at the time of the inception of the Community, as it has exercised considerable influence on the level of the tariff of the Community and of the Community's evolution during the transitional period. As a consequence there is little likelihood that there would be a general rise in tariffs during this period to the detriment of the outside world. However, the introduction of variable levies on the main agricultural products will have a similar effect to raising tariffs. In fact there has been considerable willingness to reduce tariffs in G.A.T.T. negotiations but it is not apparent that levies will be regarded as negotiable. If Britain joins the Community it will apparently have to accept the existing common tariff of the Community.

and this will mean increased duties for nearly all primary products and manufactured foodstuffs. Moreover, it is only in the form of its external barriers and not in their level that the common agricultural policy has been influenced by G.A.T.T. Of equal importance in shaping external policy has been the influence of the United States.

As indicated above, barriers to importation of foodstuffs may well be higher than before integration and this will certainly be the case if Britain joins, as British barriers to imports are much lower than those of the Six. There will be variable levies which will bring import prices up to prices that, at least in the initial stages, will be fixed by reference to the costs of production of the least efficient member state. So far as the Six are concerned this will not have much influence on their terms of trade as they have not in recent years imported appreciable amounts of these commodities. To the extent that the Six export these goods, which they are in fact likely to do with the aid of subsidy schemes in the case of wheat, the terms of trade of the Community would in fact be worsened. Britain is a heavy importer of foodstuffs and its inclusion in the Community would therefore give some scope for improvement in the terms of trade of the Community in this sector. However, Britain has been very successful in importing cheap foodstuffs and it is not clear how the complicated levy system will affect prices of imported foodstuffs; it could, in fact, have the effect of keeping prices higher though, in the absence of commodity agreements, it is more likely to send these prices lower than they
would otherwise have been.

For industrial goods the terms of trade of the Community would be improved if, due to combination within the industries, the demand and supply of the Community became centralised and advantage were taken of low elasticities of supply and demand of outside countries. This, indeed, may occur though, in relation to export trade, competition with the United States would well result in some improvement for other countries of supply conditions and prices. The question of monopoly of supply is not a peculiar feature of economic integration as there are numerous large cartels or organisations already transcending national frontiers.

There will be some goods produced in the Six and also in the overseas territories which will, nevertheless, still be imported from the outside world. In the case of trade in these products it can be expected that the terms of trade of the integrated purchasing areas will be improved whilst those of outside suppliers will deteriorate. In the primary products sector this may include beverages such as tea or coffee, bananas, vegetable oils and metals. In fact it appears that barriers to tea imports are to be eliminated in connection with the entry of Britain into the Community. In the manufactured goods sector a liberal tariff policy would minimise any deterioration of the terms of trade of outside countries.

Insofar as the Community's exports are concerned there could be gains in the terms of trade of the Community
due to the development of monopoly practices in the exporting trade. The anti-monopoly provisions of the Rome Treaty would have little effect on export cartels. (17)

It may be concluded that the Community's terms of trade vis-à-vis the outside world may improve as a result of integration but that the scope for movement is not large. More important than price movements are likely to be movements in the volume of trade and it is this aspect which is of main concern to other countries. If the price of Community exports increased because of higher rewards to labour, rather than through inefficiency or monopoly, this should be accompanied by income effects which should stimulate imports and the net effect on outside countries might consequently not be unfavourable.

Attraction of Investment

The formation of a large market including not only the Six but also associated countries, is an attraction to investment from overseas and an inducement for local capital to remain within that market rather than to be sent elsewhere. The expectation of a rapidly rising standard of living coupled with consequent increase in demand promises a very adequate return on investment within the Community and associated countries.

(17) Impact of the European Economic Community, particularly the common market, upon world trade (GATT) page 21, points out that the creation of the Coal and Steel Community did not prevent the Brussels Convention, an agreement between exporters to fix minimum prices for the export of steel to third countries.
One of the French objections to the free trade area proposals, it has been noted, was that Britain would attract investment at the expense of investment in the Six. This was because it would possess a larger preferential market than the Six. Both would have access to Europe but the Commonwealth would be a larger market than the countries associated with the Six.

Integration of the Six has indeed promoted investment from abroad notably from the United States and Britain, and between the countries of the Community. In the latter connection the provisions of the Rome Treaty for a European Investment Bank have been of relatively minor importance but should be useful in assuring the development of backward areas.

The G.A.T.T. working party on the association of overseas territories expressed some opinions as to the effect of the Rome Treaty on investment within the territories. In the case of cocoa, members of the working party noted that the nine percent tariff preference in itself would give a substantial return on the capital invested in new cocoa plantations; in addition to profits already being made in cocoa this would act as a strong further attraction for investment of private capital in cocoa growing in the associated territories. They also considered that the Investment Fund would contribute to the construction of the necessary basic services for opening up new areas within the associated territories. (18)

The reply of the Six to these views was that cocoa growing in Africa was a notion that was quite alien to the European concept of investment. Moreover, it was yet too early to say how capital available from the Investment Fund would be allotted but it would probably be devoted to the diversification of economies which were at present far too dependent on a limited number of crops. (19) Similar opinions were expressed in regard to coffee and members of the working party pointed out that Germany and Benelux had considerable experience of tropical agricultural development and that the new preferential arrangements would attract that experience and the necessary capital into the associated territories. (20) The effect of preferences on investment in tea (21) in the associated territories was also mentioned. On the other hand actual investment was considered unimportant in relation to the expansion of production of some commodities where little capital was necessary. (22) In regard to aluminium, the adverse effect of the Six's preferences on development of new projects outside the associated territories was discussed. The report expressed the view that the artificial stimulation of aluminium production in the overseas territories could prejudice Ghana's interests. Ghana hoped to proceed with the Volta project during the next few years, the sale of aluminium from which could

increase Ghana's foreign earnings by 60 percent. The project could cost some $840 million. The establishment of a common tariff on aluminium would seriously prejudice Ghana's chances of securing the funds to proceed with the Volta project. (23) Since this time there have been moves to reduce if not eliminate the preferences in the Six on tropical products and also for the association with the Community of additional countries so that the current picture is not clear.

Nevertheless, it can be said that the possible effects of the formation of the Community on investment appear to be:

- to stimulate the establishment and expansion of industries in the Six with capital derived from both the Six and from third countries which might otherwise have been invested elsewhere;
- to stimulate investment in the associated territories which might be uneconomic in the absence of a preferential market in the Six, at the expense both of investment by the Six and by outside countries elsewhere;
- consequently to retard growth in both primary production and manufacturing industry elsewhere.

The general attitude of the Six is that growth in demand in the Community should, nevertheless, in spite of the incentives to invest in the Community, assure an adequate demand for the products of third countries and therefore not

retard investment therein. In due course the Six should also become an exporter of capital.

Whether the optimism of the Six is or is not justified, the moderation of external protective barriers, such as tariffs, would reduce any adverse effects on investment in third countries.

Finally, it may be noted that one writer stresses the beneficial effects of integration on the likely pattern and nature of investment within the Community. Economies of scale and location can be better utilised. Public investment will be necessary, especially to promote the welfare of backward areas. (24) Some public investment, as has been discussed, is envisaged by the Rome Treaty.

Overall economic effects

If it is possible to make an overall assessment of the economic effects of the European Economic Community in a few words, the picture would be one primarily of expanding prosperity and standards of living in the Community itself. This would be accompanied by accelerated economic growth in the associated territories.

Insofar as stability is concerned one writer has pointed out that the large market, because of the leading role of big firms, provides better possibilities for forecasting economic changes, spreading out uncontrollable variations and ensuring some stability of expansion.

Looking at historical examples, such as America in the 1929

depression, this author, however, concludes that if a large market does, despite its larger powers of resistance, succumb to an economic crisis, the repercussions are much graver than in a smaller market (25).

In regard to the outside world, industrial countries should, after some adjustments be able to increase their trade with the Community; though their terms of trade might deteriorate to a minor extent this could be made up by increase in volume of trade. Primary producing countries have, however, little to hope for in the way of increased trade and may have to suffer diminution thereof because of greater self-sufficiency in the metropolitan countries and greater satisfaction of their needs for tropical products from the associated territories. These losses could scarcely be compensated for by cheaper imports nor does it appear likely that the losses can readily be made up by increased exports to other countries. Development in the primary producing countries would therefore tend to lag and investment to flow not to these countries but to the more prosperous Community and associated countries. Those countries that supplied raw materials not produced in the integrated area would be in a less difficult position.

British membership.

Despite a measure of responsible support in the immediate postwar period for European union in Britain, when the first move towards real economic integration took place, in the form of the European Coal and Steel Community, Britain found reasons to stay outside. It followed that she did not participate in the Messina Conference which drafted the Rome Treaties and that the latter were consequently not framed so as to take account of British interests.

The original abstention of Britain appears to have been political in motivation. Britain did not like the idea of surrender of sovereignty to European bodies. The European Economic Community was, however, a serious challenge to Britain. The Six formed a growing market for British goods; although not such an important market as the Commonwealth it was nevertheless a more rapidly expanding one. (1) Moreover, British economic growth had been persistently lagging behind growth in the Continent. It was considered that this disparity would be likely to increase if Britain were excluded from the

(1) Professor Meade has pointed out that Britain sells almost 50 per cent of her exports to the Commonwealth and only 15 per cent to the Six and that it would be rash to assert that in future years the rate of growth of demand in the Six will continue to be materially higher than that of Commonwealth countries. The U.K. the Commonwealth and the Common Market (1962) page 12. Trade and Navigation Accounts of Britain show proportions of trade to these destinations as follows:

<table>
<thead>
<tr>
<th>Destination</th>
<th>1959</th>
<th>1961</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commonwealth and Ireland</td>
<td>45.5%</td>
<td>43.1%</td>
</tr>
<tr>
<td>The Six</td>
<td>14.0%</td>
<td>16.4%</td>
</tr>
</tbody>
</table>
the process of integration taking place on the continent.

As a consequence Britain put forward the proposals for an industrial European free trade area whose fate has been described in Chapter 1. It was there noted that one reason for failure of the British proposals was that it was felt by some of the Six that a free trade area unaccompanied by other measures of economic integration involving considerable surrender of political sovereignty was impracticable because of the inequality of conditions of competition. Such conditions, it was appreciated, may quite justifiably vary because of disparity of natural resources but generally speaking the variations in Europe were not due to this cause. If anything they tended to vary obversely with natural resources. The European country with lead deposits, for example, was more likely to have a high internal price for lead than the one without deposits, because in the latter case imports were freely allowed and world prices for commodities tended to be cheaper than European costs of production. Nevertheless countries desire to utilise their resources even if imports can be obtained more cheaply. Integration was therefore likely to be accompanied by a raising of protection on foodstuffs and raw materials which was incompatible with the British concept of a free trade area.

Moreover British protection for domestic agriculture has been for many years based on a different principle to that of the Six. The Six protected their agriculture by high
external barriers and this led to high consumer prices. British protection to agriculture, though not less protective in incidence, was based on a different principle. External barriers were generally low and the domestic farmer was assisted by subsidies or deficiency payments which bridged the gap between his guaranteed price based on production costs and the price at which imports were available. Consumer prices were low and largely because of the limitations on arable and pastoral land in relation to the population, imports of most commodities were relatively high. By reason of the fact that Britain was the only open market for some commodities, exporters tended to compete for the chance to supply to the extent of selling to Britain below their costs of production. Cheap food kept down British living costs and increased her competitive ability to export manufactures. She did not wish to face the economic problems attendant on a change to the methods of the Six which involved amongst other things the purchase of French cereals at much higher prices than she could obtain outside the Six. (2)

(2) Professor Meade points out that the common agricultural policy may result in a rise of 2½ per cent to 3 per cent in the British cost of living. op.cit., page 23. Sir Donald MacDougall has expressed a similar conclusion. Britain and the Common Market, Rotterdamsche Bank Review, December 1961 page 20.
Moreover, although Britain no longer looked to the Commonwealth as the main expanding market for its exports, it was anxious not to lose ground there, whether in relation to trade or politically. To give worthwhile concessions to Europe in order to enable European countries to supply a larger proportion of the valuable British market for foodstuffs would undoubtedly diminish trade from the Commonwealth. Even the grant of free tariff entry for European goods of all types into Britain would render many of the Commonwealth preferences in the British market of little significance. There was no hope that additional markets for the majority of these products from the Commonwealth could be found on the European continent as compensation for the loss of preferences in Britain because of the trends to self-sufficiency in the Six in the agricultural sector. These considerations pointed to the likelihood that British association would accelerate the disbandment of preferences received by Britain in the Commonwealth, which are important to the maintenance of British export trade and that it would also tend to limit the purchasing power of the Commonwealth countries because of their diminished exports. These effects could well be accompanied by political disbandment of the Commonwealth.

Britain's first reaction to the refusal of the Six to entertain a free trade area was the creation of the European Free Trade Association (E.F.T.A.) described in the following chapter. This association, often referred to as the
Seven, attempted to negotiate with the Six, notably in a working party of O.E.E.C. These negotiations were cumbersome and after some delay Britain entered into direct negotiations with the Six.

The Six were not so eager as Britain to find a solution to the problem of overall European integration and were more concerned to weld their own instrument into a successful unit. (3) Moreover the Rome Treaty was not easily adaptable to British requirements. (4) Some tariff reductions and quota relaxations were made by the Six but whether this was an attempt to hold open the door for integration or to make Britain and the other Europeans less dissatisfied with their lot outside the Community, is not clear.

However, in Chapters 3 and 4 the conclusion was reached that the effect of integration would be predominantly trade-creating in the industrial sector. There would, admittedly, be a considerable degree of trade diversion as the integration of the Six proceeded and therefore a considerable structural readjustment in the composition of the imports of the Six but confidence was felt that overall industrial imports would continue to rise. In these circumstances why did Britain not feel strong enough to take advantage of the expanding market of the Six over the barrier of the common

(3) This was the French attitude which prevailed over that of some other members of the Six. (4) This was eventually solved by saying that Britain would have to accept the Treaty as it stood.
external tariff? By staying outside the Community she would at least escape the inflationary effect of higher food prices and might improve her competitive position vis-a-vis the Six in the markets of third countries such as the United States as inflationary effects developed in the Six. (5) Moreover she could lend her weight to that of the United States in negotiating reductions in the level of the common tariff of the Six, a process that the Six are by no means unwilling to undertake. (6) Recent trade figures bear out the proposition that Britain's exports to the Six can in fact be expanded from her position outside the Community.

It is not easy to answer these contentions. There had long been in Britain a section of opinion strongly in favour of joining the Community and this section was given added strength when Mr. Thorneycroft rejoined the British cabinet. More important, however, was the attitude of the United States which, apparently for political reasons related to defence, decided to throw its full weight behind the idea of British membership. Whilst furthering its political aims of a unified Europe, the United States also saw in British membership an opportunity to further its economic aims expressed in the Atlantic Charter, Article VII of the

(5) Such influences have developed in Germany, formerly the competitive member of the Six par excellence. (6) Professor Meade has pointed out that joining the Six is not the only method of bargaining substantial tariff reductions. Op.cit., page 16.
Anglo-American Mutual Aid Agreement and the G.A.T.T. of eliminating discrimination in trade or, to put this more specifically, to abolish the British preferential system.

Sir John Crawford, who has examined this question in detail, appears to attach most importance to the political reasons for Britain's changed policy. In this connection he has put forward the view that, having failed in its free trade area plans, Britain has had to re-examine old prejudices. In so doing it has come to the conclusion that there is room for manoeuvre within the scope of the Rome Treaty which, in any case, is expressed to have economic rather than political aims. (7) On the economic side Sir John Crawford considers the advantages questionable though he attaches a great deal of importance to Britain's failure to maintain economic growth outside the Community. (8) He does not consider the possibility of Britain overhauling its economy outside the framework of the Community. This is a question posed by Sir Donald McDougall, who asks whether Britain really needs this external stimulus to put its house in order, but he does not provide the answer. (9) E.J. Mishan thinks it strange that it should be generally assumed that the requisite discipline to effect modernisation of industry must necessarily

come from a common market bureaucracy rather than from the British themselves. (10). A further point mentioned by Sir John Crawford is the attractiveness of the Community to United States investors and in fact also to British investors as compared to investment in Britain. (11)

Although doubts may be expressed as to the validity of the economic arguments in favour of Britain joining the Community this is not to deny that from the point of view solely of industrial integration the association will be trade-creating. M.E. Kreinin has computed the degree of competition between the two unions, E.E.C. and E.F.T.A. and has found them highly competitive, particularly in the field of manufactures, machinery and chemicals. Undoubtedly to a very large measure this competitiveness is due to the similarity in the industrial structure of Britain and some of the Six. Kreinin found that about two thirds of the exports of both E.E.C. and E.F.T.A. are competitive with each other. (12) If the association between Britain and the Six were confined to an industrial free trade area there would be little difficulty in accounting for British enthusiasm. It is rather the association with industrial free trade of the difficult agricultural adjustments and the loosening of the Commonwealth tie that produces a mixture whose palatability to Britain is

not easily explained.

The limitation of preferential access to the British market for products of the Commonwealth, the increase of duties on such products which now mostly enter free of duty and the preferential access for European agricultural produce will, besides causing considerable diversion of trade, have economic effects that overall are unlikely to be favourable. Generally speaking the Commonwealth is a more efficient producer of agricultural produce than Europe so that there is likely to be a net loss of welfare by substituting European for Commonwealth produce. This is not to deny that the continental farmer may well be poorer than the Commonwealth farmer so that an incremental increase in his welfare may be more valuable than a similar increase in that of the Commonwealth farmer but the low income of the continental farmer is mainly due to structural reasons and needs to be solved by structural improvement and movement away from the land. Apart from these welfare effects Britain will have to pay more for its food imports and apparently much of the levy collected will be used to subsidise the export of continental surpluses to outside destinations.

Membership of the Community will entail considerable adjustments for British farming but these adjustments will be no more serious than those the Six are attempting to undertake between themselves. The Six are still a long way off from having a common producer price for such items as wheat and butter. Horticulturalists and fruit growers will
probably feel the impact of the common market the most but the elaborate grading system being introduced by the Six for fruit must tend to moderate competition. Higher prices to consumers will, at least until personal incomes correspondingly increase, result in decreased consumption of farm produce other than cereals. However, except in the case of one or two commodities such as eggs, British farmers only produce a small proportion of British consumption so that a reduction in the latter need not of itself entail a reduction in the level of production.

Professor Meade has pointed out that association of Britain with the Community can only be beneficial to Britain if the stimulus of the wider market can be combined with financial conditions which do not require Britain to restrict investment and demand in general to prevent a balance of payments crisis. A wide market without stagnation is needed.

(13) The British balance of payments will be under strain for the reasons already noted, viz. loss of Commonwealth markets, higher prices for food imports and contributions towards export subsidies for continental produce, whilst rises in the cost of living may make it difficult to hold other markets as well. Sir Donald MacDougall is of the opinion that there is more potential for loss of British export trade to E.F.T.A. and the Commonwealth than there is for gain of trade to the Six whilst there is a likelihood of substantial increase in imports into

(13) J.E. Meade, op.cit. page 16
Britain from the Six. (14) However, perhaps strains within the Community itself should not be exaggerated as they can be moderated by exchange and other adjustments as the Six have demonstrated to date. Meade, in fact, concludes that there will need to be a more frequent recourse to variations of exchange rates between the national currencies (15).

In due course it may be that the Community will move to a common currency. If this is the case, Meade points out that there will need to be a considerable further loss of economic sovereignty to ensure that this does not lead to severe deflation by areas of the Community which are losing reserves. (16) It is in fact necessary for areas in surplus to inflate whilst the deficit areas deflate. If the Community as a whole is in persistent deficit or surplus, Meade sees a necessity for alteration of the exchange rate vis-à-vis the outside world of the common currency. He considers alternative measures such as import restrictions would present overwhelming difficulties. (17) It would for instance be impracticable to limit imports from associated territories and any restrictions on industrial imports from outside countries might have serious effects on the competitiveness of industrial production of the Six in the export market.

Having examined the pros and cons of British association it is necessary to agree with most writers that the economic benefits accruing to Britain from such association are doubtful. The urgency with which the British Government is pursuing this question of joining the Community suggests rather that advantages are to be obtained in the political and defence sphere which Britain cannot afford to neglect.

Association of other European countries

Greece has already concluded an agreement of association with the Community and hopes eventually to become a full member. Denmark, Norway, Ireland, Portugal and possibly Spain may become full members whilst Sweden, Switzerland and Austria cannot face the political implication of full membership but may become associated with the common market. Turkey may also become associated but Israel and Iran, although interested to do so are unlikely to be accepted. The difficulty with Israel stems largely from its troubles with the Arab world, with which the Community is closely connected. Finland would no doubt like to be associated but Russia's insistence on the same treatment as the Six would receive appears to make this impracticable as the Six are insistent that associated European countries adopt the common tariff. The implications for a united Scandinavia of these moves are unfortunate as only Denmark and Norway are likely to be in the same position vis-a-vis the Community.

There are quite obvious economic advantages for many
of these countries in being associated with the Six as they are important producers of agricultural produce consumed by the Six such as dried vine fruits, cereals, meat, dairy produce, wine and tobacco. The advantages will be greatly increased if Britain accedes as these countries will be able to replace Australia, New Zealand, Canada and South Africa as preferential suppliers to the British market. In the case of products covered by the common agricultural policy proper, that is where protection is afforded by variable levies, the advantages that could accrue to associated countries appear unlimited. In other cases direct trade advantages should be limited to the external tariff. Greece in its association agreement has obtained a guarantee against reduction of the common tariff of 8 per cent on dried vine fruit which will be very significant if Britain joins the Community.

However, few of these countries have not some industrial ambitions and in fact a need to maintain industry in order to employ the population. In the case of a well situated country such as Denmark there seems nothing to prevent industry establishing itself there rather than in the Six whereas in the case of Sweden and Switzerland the special competence in certain types of production will no doubt ensure continued industrial activity. In the case of remote areas of the Community, well away from large population centres, such as Norway and to a less extent Greece the future of industry appears more uncertain as there would seem to be advantages in
concentration of industrial production nearer the large centres of demand and the supply of outlying areas from these centres.

In this connection it is particularly interesting to consider the case of Greece as the existence of a defined association agreement clarifies the position to some extent. In the first place it is noteworthy that Greece has 22 years before she is required to remove all barriers to industrial trade whilst she obtains free access to the market of the Community much earlier, probably now by 1970. Secondly she is to receive considerable assistance from the Community in the form of capital for modernisation of industry. Thirdly special facilities have been provided in the agreement for her to do bilateral deals with communist countries and insofar as exports are concerned it is relevant that Greece is well placed to become a centre for export to the near East. Moreover during the period of association there will be no free movement of labour to and from the Community so that if the Greek economy continues to lag there may be scope for export of labour-intensive goods such as textiles to the Community. If all else fails there is surely also the possibility that a measure of industrial protection could be retained by Greece beyond the period of association now envisaged so that in fact she becomes a sort of "associated territory."

The association of these countries will on the
whole impose some economic burdens on the Six and present problems, particularly on fitting them into the common agricultural policy. Any advantages to the Six will be long-term; if the association achieves its object the additional countries should prove valuable markets. The advantages to the countries themselves are obvious but they are offset by disadvantages to other countries such as those of the Commonwealth, assuming British membership of the Community.
Chapter 6

The European Free Trade Association

The communique of 20th November, 1959 issued in Stockholm at the time of the signature of the treaty of association by representatives of the governments of Austria, Denmark, Norway, Portugal, Sweden, Switzerland and Britain states that the purposes of the association are economic expansion, full employment, the rational use of resources, financial stability and a higher standard of living. It is asserted that the convention will establish a free market between its members, to be achieved by the abolition of tariffs and other obstacles to trade in the industrial products of member states over a period of ten years or earlier if so decided. Each country will be free to decide its own external tariffs. Free trade between the participating countries, states the communique, will stimulate competition and economic expansion. The convention assures that the effects of the removal of barriers to trade will not be nullified by means of subsidies, practices of state undertakings, restrictive business practices and limitations to the establishment of enterprises. The convention also covers agricultural goods for which special provisions are made and agreements concluded so as to promote expansion of trade and to ensure a sufficient degree of reciprocity to the countries whose main exports are agricultural. To the same end there are also special rules for trade in non-processed fish and
marine products.

The communique refers to the fact that other countries may accede to the convention and welcomes the interest of Finland in finding ways and means of participation. It also reaffirms the determination of the seven member countries to facilitate a wider multilateral association including the European Economic Community and a resolution annexed to the communiqué affirms this in some detail. A council of ministers is to be established to supervise the application of the convention.

The association, unlike the Rome Treaty, covers only the metropolitan territories of the members\(^{(1)}\) except for the Faeroe Isles, Malta, Gibraltar and Greenland.\(^{(2)}\)

A programme of reduction of duties on trade between the member states provides for their reduction by 10 per cent per annum so that they are eliminated by January 1970.\(^{(3)}\)

Reduction of internal duties has been accelerated so as to keep as far as possible in line with the internal reductions made in the European Economic Community. By

\(^{(1)}\) Article 1. \(^{(2)}\) Article 43(2) and Annex F. \(^{(3)}\) The first two-year reduction of twenty per cent took place on July 1, 1960. The schedule provides for reduction by fifty per cent by January 1, 1965. (Article 3).
October 1962 internal duties had been reduced by 40 per cent and at the end of that month five member states made further reductions of ten per cent. This was to be followed during the course of the next few months by reductions by the other two member states, Austria and Norway so that all member states will have reduced internal duties by fifty per cent.

In May, 1963 the Council decided that duties would be reduced by sixty per cent of 1963 and Owing to the absence of a common external tariff, duties should be completely substituted by rules of definition of origin, to define when goods are deemed to have originated in the area, have assumed considerable significance as there is no free passage of goods between member states of goods originating from outside the area. Three qualifications are specified, either that the goods have been wholly produced in the area, or that the goods are of a type specified in the list of processes annexed to the Convention and that they have been subjected to a specified qualifying process in the area or, thirdly, that they have been produced in the area and that the value of the imported materials does not exceed fifty per cent of the export price of the goods. (4) There are, however, two qualifications to the last-mentioned criterion. It does not apply at all to certain goods listed in Schedule II of the list of processes. These goods are all in the textile field and it is understood that the exclusion of the percentage rule is designed to discourage the re-export within the area of textiles of

(4) Article 4 (1).
low value imported from Asia on which an insubstantial process may have been performed. Secondly, certain listed basic raw materials are, for the purposes of the percentage rule, deemed to be of area origin although in fact they have been imported from outside. Apart from the special device for textiles, the rules are similar to those earlier proposed by Britain for the wider free trade area.

The origin rules are not considered sufficient to meet all the problems likely to be caused by differing external tariffs. Article 5 recognises that deflections of trade may be caused where there are significant differences in external tariffs on raw materials for intermediate products. In such cases the Council may authorise an affected member to safeguard its position and it may recommend remedial measures such as amendment of the origin rules. (5) Moreover, member states intending to reduce external duties are asked to notify the Council and to entertain representations from other member states who fear that these reductions may lead to deflections of trade. Some fears were expressed by other members of the G.A.T.T. that these provisions would inhibit reductions in external duties and contribute to increases in external tariffs. (6)

Revenue duties and internal taxes are to have any protective element removed. (7) Any goods on which drawback has been paid by a member state are ineligible for area treatment. (8)

This provision is intended to maintain the applicability of the external tariff of the exporting member state to the imported components of the exported product. Export duties are forbidden on trade between member states. (9)

Quantitative restrictions are not to be introduced or intensified on products from other member states, are to be administered equally vis-a-vis all other member states and quotas are to be globalised and progressively increased in a manner rather similar to that provided for in the Rome Treaty. Apart from Austria and Norway the Seven maintain few import restrictions and progress by these two countries in removal of restrictions in accordance with the Convention has been reported. Subject to the control of the Council the rule regarding elimination of import restrictions may be departed from in case of balance of payments difficulties. (11) Quantitative export restrictions are also to be abolished. In answer to a questionnaire from other members of the G.A.T.T., the member states said that they considered that they were entitled to expand quotas more rapidly between themselves than they relaxed restrictions on such goods from other G.A.T.T. members but that they did not intend to use quantitative restrictions to create a preferential area amongst themselves. (12)

There are provisions for governmental aids to exports to other member states (13) and for removal of protective elements in state trading practices. (14)

Action may be taken against dumped or subsidised imports. (15) Moreover, subsidies on exports of agricultural goods to any destination should not be applied so as to damage the interests of other member states. (16) Enterprises are not allowed to take advantage of a dominant position or to make agreements to restrict or distort competition within the area. (17) The right of establishment is confined to the abolition of restrictions on establishment that frustrate the benefits expected from the removal of trade restrictions. (18)

Subject to some control by the Council, member states may take restrictive measures against imports from other member states where increased imports have resulted in unemployment in a sector of industry. (19) The Article is intended to deal with transitional difficulties and any measures taken should be temporary. (20)

Generally speaking, the Convention does not apply to trade in agricultural goods. (21) The member states have, however, subscribed to some general provisions regarding agricultural policy (22) and have agreed to consult on trade in agricultural goods. (23) There are also provisions regarding export subsidies. (24) Moreover, at the instance of Denmark, the Convention provides for the possibility of bilateral agreements on agriculture between member states. (25) Under this provision Denmark has concluded bilateral agreements with Austria, Sweden, Switzerland and Britain. (26) Under the trade agreement with

Britain, the latter has agreed to abolish import duties on bacon, canned pork luncheon meat, blue vein cheese and canned cheese from all sources. Denmark has also some rights of consultation on dumping and subsidies. (27) The agreement with Sweden contains a novel provision of a discriminatory nature, under which a proportion of Swedish duties collected on certain meats, dairy products and potatoes imported from Denmark is refunded to Denmark; an ingenious way of creating a new preference. (28) The agreement with Switzerland provides for the abolition of customs tariffs on certain fish from all sources. It also provides for the increase of quotas available to Denmark on certain animals and meats and cereal seeds. In regard to cattle and beef, the obligation is to increase the Danish share of imports. Denmark is also assured a forty per cent share of the Swiss market, to be effected if necessary by restricting imports whose price has been reduced by subsidies below world market prices. (29) Except in the case of Britain the agreements appear to have a discriminatory element. The Danish view on these agreements is that that they would have preferred to have had free trade in agricultural products in the area but have been obliged to settle for what they would get. Concurrent with the association of Finland with the E.F.T.A., the Danes signed an agreement with that country under which quotas of certain agricultural products from Denmark are assured entry into Finland and duties on certain agricultural products originating from E.F.T.A. countries are to be abolished. In February 1962 an agricultural agreement was signed between Portugal and Switzerland.

The exclusion of agriculture from the free trade area and the nature of the Danish agreements has led to considerable criticism in the G.A.T.T. The Seven have there argued that the freeing of some agricultural imports from import duties has raised the percentage of trade on which duties will be eliminated so that ninety per cent of the intra-association trade will be free. (30) This, it is argued, satisfies the G.A.T.T. requirements that "substantially all" the trade within the area shall be free. (31)

Trade in fish and marine products is also generally excluded from the Convention but it is provided that it shall be the subject of study by the Council. (32) Britain has agreed with Norway to treat for ten years a tariff quota of frozen fish fillets from Scandinavian countries in the same manner as industrial goods.

The Convention contains short provisions on invisible transactions and transfers (33), economic and financial policies (34) and provides for a general consultation and complaints procedure. (35) These provisions are of a more superficial nature than those in the Rome Treaty. In May, 1963 the Council decided to set up an Economic Development Committee to promote development of the more backward members of the association.

Annex G to the Convention provides a number of special safeguards for Portuguese industry. Except for goods important in export trade and any other goods notified by Portugal, customs duties need only be reduced by 50 per cent by 1 January, 1970, the subsequent timetable for reduction to be set before that date but so that all duties will be eliminated on area products by 1 January 1980. Moreover, up to 1 July 1972, new duties

(30) G.A.T.T. document L/1167 - op. cit. answers to questions 4 & 5.
may be introduced to protect developing industries. In addition, export restrictions may be applied on minerals if necessary to protect raw material supplies for local industry.

The Convention applies to Liechtenstein so long as that country maintains a customs union with Switzerland.

In March, 1961 Finland signed a treaty of association with the E.F.T.A. As noted in Chapter 1, this treaty in effect makes Finland a member of E.F.T.A., though there are separate institutional devices that distinguish the association from full membership. Finland is also granted some very limited derogations from the timetable for elimination of duties and is allowed to retain import restrictions on a limited number of products. There are also some minor reservations by Finland on capital movements and import liberalisation. Under an agricultural agreement Finland guarantees Denmark certain quotas on bacon and pork, beet sugar, apples, pears and apple pulp and undertakes to remove duties on beet sugar (to be reviewed in 1965), apples and pears (seasonal), apple pulp, a number of seeds, nursery shrubs and bulbs (duty free quota) coming from all E.F.T.A. countries. There are also provisions regarding casings and vegetables.

In accordance with an E.F.T.A. decision of 31 July, 1961, all member states have now made application to the E.E.C. for a form of association or membership of the Community. Britain and Denmark applied to full membership in August 1961; Austria, Sweden and Switzerland made application for negotiations with a view to association with E.E.C. in December 1961. In May, 1962 Norway applied for full membership and in June 1962 Portugal applied for "collaboration."
Economic consequences

The original British proposals for a free trade area embraced all O.E.E.C. countries. These countries included states in different stages of industrialisation and problems regarding the protection of infant industries that were less industrialised than the others, the provision of funds for economic development and assured markets for agricultural produce would all have arisen. All these problems have in fact been tackled in the Greek association with the Community.

The European Free Trade Association itself comprises a varied collection of industrialised and semi-industrialised countries. Apart from some additional time in which protection may be granted the association appears to do nothing to assist the growth of industry in Portugal and no special provision has been made for Norwegian industry, the development of which was regarded in 1950 as a stumbling block to plans for a Nordic customs union. (36) Austrian industry will enjoy some protection, at least from British industry, by reason of its geographic location.

Two reasons appear to have motivated the Seven to form their rather diverse and far-flung union. First, some advantages were seen in the way of additional trade, these advantages were more likely to be due to the preferred position the members would enjoy in the markets of each other than to any increase in competition in the area. In view of the lack of provision for movement of labour and capital and for a common tariff it appears that the principle of comparative advantage will apply. Under this principle exchange rates are set that tend to minimise (36) Chapter 1, page 12.
differences in the money cost of production between the different countries. It does not therefore follow that there will be a general movement of industrial production from one country to another but rather that real wages will vary from one country to another according to the relative efficiency of production generally in each country. In order to maximise this efficiency there will be some concentration in each country on the relatively most efficient lines of production and this specialisation will in due course lead to increase in trade within the area. Unless, therefore, individual sectors of industry have been relatively over-protected so as to distort the economic pattern or the relative efficiency of competitive production in the area is very different from that offered in the market by the world as a whole, there is no reason to anticipate a great deal of additional trade merely because industry in Britain is more efficient than industry in Austria and the two are both members of the Association. As Scitovsky has pointed out (37) the extent of international reallocation is bound to be smaller than it would be if output were always concentrated in enterprises with the highest labour productivity.

The second advantage foreseen was an improvement in negotiating power with the Six. It was thought that if the Six saw their trade with the area diminishing they would be more likely to come to terms. It was also thought that association with the Community might be a more difficult task if too rigid a structure were created and in fact the Association has a very loose structure.

(37) T. Scitovsky, Economic Theory and Western European Integration, (1958), page 44. Scitovsky appears to think that this principle would hold even in an union as close as the European Economic Community, but this is more doubtful.
Whereas the European Economic Community may be trade-creating as well as trade-diverting the Free Trade Association appears to be mainly trade-diverting and therefore cannot be expected to lead to an increase in overall economic welfare. However, it may nevertheless have given the economies of the member states some welcome support needed in view of the impact of the creation of the Community.

The following are some approximate percentages of origin and destination of trade during 1956 (38):

<table>
<thead>
<tr>
<th>Exports of Six</th>
<th>Imports of Six</th>
<th>Exports of Seven</th>
<th>Imports of Seven</th>
</tr>
</thead>
<tbody>
<tr>
<td>Six,</td>
<td>31%</td>
<td>27%</td>
<td>22%</td>
</tr>
<tr>
<td>Britain,</td>
<td>6%</td>
<td>5%</td>
<td>7%</td>
</tr>
<tr>
<td>Rest of Seven</td>
<td>17%</td>
<td>10%</td>
<td>12%</td>
</tr>
</tbody>
</table>

The figures for the Seven can be further broken down as follows:

<table>
<thead>
<tr>
<th>Exports of rest of Seven</th>
<th>Imports of rest of Seven</th>
<th>Exports of Britain</th>
<th>Imports of Britain</th>
</tr>
</thead>
<tbody>
<tr>
<td>Six,</td>
<td>35%</td>
<td>43%</td>
<td>13%</td>
</tr>
<tr>
<td>Commonwealth *</td>
<td>-</td>
<td>-</td>
<td>45%</td>
</tr>
<tr>
<td>Britain</td>
<td>16%</td>
<td>13%</td>
<td>-</td>
</tr>
<tr>
<td>Rest of Seven</td>
<td>13%</td>
<td>10%</td>
<td>10%</td>
</tr>
</tbody>
</table>

* Not calculated for 'rest of seven'.

These figures show that trade of the Seven with each other is less important than trade between them and the Six. This is particularly so for the members of the Seven other than Britain.

(38) Source. O.E.E.C. Network of Intra-European Trade, 1956. These figures do not include associated overseas territories.
The figures also indicate the importance of the Commonwealth in British trade.

Whereas the exports of the Six to all destinations under consideration are primarily of manufactured goods as is also the case with Britain, those of the other members of the Seven are more diversified, foodstuffs and raw materials being more important, taken separately, than manufactures in their exports to Britain and in the aggregate, than exports of manufactures in their exports to the Six. About one quarter of British imports from the Six are of foodstuffs.

The figures indicate that trade between the Six is more competitive in nature than between the Seven and is also more important. It appears likely that the formation of E.F.T.A. will lead to expansion of trade between the Seven in products formerly imported from abroad than in competitive products. Such expansion may be largely at the expense of the Six.

The E.F.T.A. therefore appears to be a move primarily of struggle with the Six, probably more of a defensive nature than an offensive one, inspired by prospect of loss of trade with the Six. In this struggle Britain appears to be the strongest member with 13\% per cent only of its exports going to the Six; the Six have to maintain heavier exports to the Seven, 23 per cent of their trade, whilst the rest of the Seven are vulnerable to the extent of 35 per cent of their trade. If the Association were to survive as a viable institution it appears that Britain would need to take more of the produce of the Seven than at present.

The tentative conclusions enunciated above may usefully be examined in relation to the economic propositions put forward.
by a number of writers which have been discussed in earlier chapters relating to the European Economic Community.

Meade's first proposition, that integration is more likely to lead to a net increase in welfare if the economies of the partner countries are actually very competitive or similar but potentially very complementary or dissimilar, which is linked with the maintenance of high duty rates of each other's products, does not appear to offer much hope for increased welfare in the Association. The economies of the Seven do not appear at present to be very competitive nor would it seem that most of the existing trade is subject to high duties, nor do duty rates vary greatly as between the various countries. One author quotes figures of average tariff rates in the Seven of from 9 per cent to 12 per cent whilst in the Six the average tariff rates are stated to be from 9 per cent to 25 per cent. He states that the results are similar if the overall figures are dis-integrated. (39) The same author has examined the ratio of the value of exports to the value of imports of the individual members of the Seven (except Switzerland, for which suitable figures were not available) for groups of commodities and has concluded that a high ratio shows that a country has a comparative advantage in production of a commodity. As a result he has found that only four per cent of the exports of the Seven (except Switzerland) were of commodities in which three or more countries had a comparative advantage; 15 per cent where two countries had a comparative advantage and 76 per cent were of exports of commodities in which only one country had a comparative advantage. The 76 percent was composed of

(39) M.E. Kreinin, The Outer Seven and European Integration; American Economic Review, June, 1960, pages 374/5.
55 per cent where Britain had the comparative advantage, 14 per cent Scandinavian countries and 7 per cent Austria or Portugal. The share of Britain was mainly in the sectors of chemicals, machinery and manufactures. The author concludes that the figures show the extreme complementarity of the E.F.T.A. and indicates the ease with which it could be established. (40) This conclusion reinforces those already arrived at to the effect that trade-diverting effects are likely to be predominant in the Association.

Examination of E.F.T.A. trade figures for 1961 show that trade between E.F.T.A. countries other than Britain had expanded over the 1956 proportions of trade but that most of the proportionate expansion had taken place in 1958 before the formation of the Association. On the other hand trade between other E.F.T.A. countries and Britain had not increased over the former proportions. Trade between E.F.T.A. countries and the Community (including Greece) had, however expanded to a greater degree than trade between E.F.T.A. countries. (41). During 1961, as compared with 1960, E.F.T.A.'s exports to the Community rose by 11 per cent whilst trade between E.F.T.A. countries rose by 9 per cent. Imports of E.F.T.A. countries from the Community rose slightly more than imports from each other. (42) The figures do not include Finland.

The above figures, being based only on selected years, are not conclusive but appear to indicate that in practice the E.F.T.A., insofar as it had developed by 1961, had not in general diverted trade internally as compared to trade with the Community.

Chapter 7

The European Economic Community and the European Free Trade Association

Effects on Australia

(a) Direct Trade Effects

(i) Exports

The pattern of Australia's export trade in recent years has been as follows:

<table>
<thead>
<tr>
<th></th>
<th>TOTAL</th>
<th>Britain</th>
<th>The Six</th>
<th>Seven (x)</th>
<th>Peripherals (y)</th>
<th>Other Destinations</th>
</tr>
</thead>
<tbody>
<tr>
<td>All exports (z)</td>
<td>873.1</td>
<td>229.7</td>
<td>160.4</td>
<td>8.7</td>
<td>7.6</td>
<td>466.7</td>
</tr>
<tr>
<td>Animal substances</td>
<td>369.8</td>
<td>70.8</td>
<td>123.7</td>
<td>4.5</td>
<td>5.2</td>
<td>165.6</td>
</tr>
<tr>
<td>Minerals</td>
<td>29.3</td>
<td>3.9</td>
<td>3.8</td>
<td>0.4</td>
<td>-</td>
<td>21.2</td>
</tr>
<tr>
<td>Sub-total</td>
<td>399.1</td>
<td>74.7</td>
<td>127.5</td>
<td>4.9</td>
<td>5.2</td>
<td>186.6</td>
</tr>
<tr>
<td>Animal foods</td>
<td>136.0</td>
<td>68.8</td>
<td>3.9</td>
<td>0.3</td>
<td>0.1</td>
<td>62.9</td>
</tr>
<tr>
<td>Vegetable foods</td>
<td>180.0</td>
<td>61.3</td>
<td>19.6</td>
<td>2.6</td>
<td>2.1</td>
<td>94.4</td>
</tr>
<tr>
<td>Liquors</td>
<td>2.2</td>
<td>0.8</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>1.4</td>
</tr>
<tr>
<td>Vegetable substances</td>
<td>1.0</td>
<td>0.1</td>
<td>0.2</td>
<td>0.1</td>
<td>-</td>
<td>0.6</td>
</tr>
<tr>
<td>Animal fats</td>
<td>4.6</td>
<td>0.6</td>
<td>0.1</td>
<td>-</td>
<td>-</td>
<td>3.9</td>
</tr>
<tr>
<td>Marine oils</td>
<td>1.0</td>
<td>0.3</td>
<td>0.6</td>
<td>0.1</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Leather</td>
<td>3.8</td>
<td>2.6</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>1.2</td>
</tr>
<tr>
<td>Timber</td>
<td>4.0</td>
<td>0.8</td>
<td>0.1</td>
<td>-</td>
<td>-</td>
<td>3.1</td>
</tr>
<tr>
<td>Metals, manufactures thereof and machinery</td>
<td>87.8</td>
<td>16.0</td>
<td>2.9</td>
<td>0.2</td>
<td>0.2</td>
<td>68.7</td>
</tr>
<tr>
<td>Sub-total</td>
<td>420.4</td>
<td>151.3</td>
<td>27.4</td>
<td>3.3</td>
<td>2.4</td>
<td>236.0</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>53.6</td>
<td>3.7</td>
<td>5.5</td>
<td>0.5</td>
<td>-</td>
<td>43.9</td>
</tr>
</tbody>
</table>

NOTES: (x) 'Seven' comprises Austria, Denmark, Finland, Norway, Portugal, Sweden and Switzerland;
(y) 'Peripherals' comprises Greece, Ireland, Spain and Turkey;
(z) 'All exports' comprises all trade except non-commercial items and gold

Source: Overseas Trade Bulletin (calculated).
In the above table exports have been divided into three broad categories. The first category comprises wool, hides and skins, pearl shell and minerals. These products are not, generally speaking, subject to any protective devices in the Community. The second category comprising foodstuffs, leather, timber, metals and manufactures will be subject, with minor exceptions, to protective barriers. The third or miscellaneous category, whose largest component is petroleum products, is relatively unimportant in regard to Australian export trade to Europe. Although there is no clear cut boundary between products at risk and those not at risk, subsequent examination will show that the trade with Europe comprised in the first category can be regarded as not at risk and that in the second category as being at risk. There are some small items which could be transferred from one category to another depending on the assumptions made but their size enables an assumption to be made that any transfers would be largely self-balancing, i.e. what one category loses in amount, the other would gain.

It is fortunate for Australia that, with the exception of a few small countries such as Norway and Portugal, whose capacity to produce is relatively unimportant, western European countries do not encourage the production of wool. As a consequence the common external tariff in the Community is free though there is a small protective tariff on spun wool (i.e. 'tops'). There is also no tariff on hides and skins nor on shells. In the Free Trade Association the only tariffs are those of Portugal and Norway. The formation of the
Community and the Association should therefore have no direct trade effects on Australian exports of wool, shells or hides and skins to Europe. The present tariff position is not immutable and if, as is likely, there is a heavy increase in the availability of cattle hides due to increased beef production it may be that some protection will be afforded. However the demand position for hides should increase in strength so that no diminution of imports results. None of these items are dutiable in Britain so that no preferential position will be lost.

Indirect effects on trade in these items can include changes in total demand, in particular growth in demand through income growth, and substitution effects.

Likely indirect effects on Australian trade in wool have been studied by R.J. Cornish.\(^1\) This study has particular relevance to the Six but can be applied also to Britain.

In this study Cornish examines the likely increase in income per head in the Community. He then considers the likely effect on demand for woollen textiles and points out that this should be larger if increase in income occurs where income is currently low rather than where it is already high. His conclusion is that consumption of woollen textiles over the first twenty years of the Community's existence could increase by about 25 per cent to 30 per cent per head. He points out that existing tariffs on synthetic yarns and fibres are higher than those on wool. For this reason integration is

\(^1\) R.J. Cornish: The proposed Free Trade Area and Western European demand for wool. Quarterly Journal of Agricultural Economics. July, 1957. (Dept. of Primary Ind.) pages 153/160.
likely to result in a greater increase of competition in the synthetics industry than in the woollen industry with corresponding price advantages to the synthetic product. He does not appear to consider resultant economies of scale of much importance in either industry, taking the view later expressed by Dell(2) that the existing markets are in general large enough to permit most of the economies of scale that would be possible in an integrated market. Cornish takes the view that the European climate will continue to assure a strong preference for pure wool as against synthetic fibres. This he contrasts with American experience where synthetic fibres have captured a considerable share of the market to the exclusion of wool. He considers that it is difficult to estimate the long-term reduction in demand for wool fabrics that might be brought about by change in the relationship between wool and synthetic prices but that it is unlikely to be more than 5 per cent to 6 per cent. The net outlook for wool consumption per head therefore still remains favourable.

The G.A.T.T. secretariat (3) has estimated the import of natural textile fibres, amounting to 1.3 millards of dollars per annum in 1953/55 as 1.25 milliard dollars, at constant prices, per annum in 1973/75, assuming gross national product in 1973/75 is 190 per cent of the 1953/55 levels. This estimate is, however, increased to 1.45 and 1.65 milliard dollars if the assumption as to G.N.P. is raised to 220 per cent.

and 250 per cent respectively. Assuming a growth rate of 3.5 per cent per caput G.N.P. should rise nearly to the middle estimate (4) which if the G.A.T.T. Secretariat's assumptions are correct, will mean an increase in demand for wool of about ten per cent.

Cornish's estimate of increase in income per head is, however, only from 49 per cent to 81 per cent over this period so that his estimate of an increase in wool consumption per head is optimistic in comparison to the G.A.T.T. study, which assumes a decrease in imports of natural fibres at a gross national product increase of ninety per cent. The fact that the conclusions of Cornish are expressed per head whilst the G.A.T.T. study takes account of population changes (4) may assist in reconciling the conclusions. The G.A.T.T. study does include also such fibres such as cotton which may be more vulnerable to substitution than wool. From the above studies the general conclusion may be reached that wool imports of the Six are not likely to decrease and may increase.

The formation of the Community, it has been noted, brings into effect two opposing influences on the demand for wool, an income effect which increases demand and a relative price effect which decrease it. If the Six had continued without integration both these influences would have made themselves felt to lesser degrees than will be the case. There is no reason to feel that integration has altered the balance unfavourably and it may be that the income effect will outweigh the price effect so that the effect of integration proves favourable.

(4) A growth in population of 11 per cent over the period is assumed.
Another question that may be asked is whether, if Russia becomes an important exporter of wool, integration will tend to make the countries concerned take more or less wool from Russia than if no integration had taken place. This question cannot be answered but it appears at present that the Community is less likely to enter into bilateral deals than some of the individual members of the Six were prone to do and as Russia, at least at present, conducts much of its foreign trade on this basis, the assumption may be made that integration would not lead to redirection of trade to Russia from Australia.

In regard to minerals there are possibilities for production increases in the associated countries and also prospects for increase in usage. The net effect of these developments on demand for imports from Australia is difficult to evaluate. One favourable indirect effect arises from the fact that due to the tendency of freight costs to rise and also to the development of smelter capacity in Australia, it is likely that Australian exports of some minerals will tend to disappear and that instead it will be sought to export the smelted metal. This seems particularly important in relation to the Community in regard to zinc where at present concentrates of ores are exported. However, the Community, though it allows free import of ores, has a protective tariff on the metal, so that the prospect of continuing exports of zinc to the Community are reduced by the trends in this trade.
The percentages of Australian export trade to the destinations under consideration covered by the abovementioned commodities and the commodities which hereafter will be shown to be at risk and the miscellaneous group are as follows:

<table>
<thead>
<tr>
<th></th>
<th>Britain</th>
<th>Six</th>
<th>Seven</th>
<th>Peripherals</th>
<th>Total</th>
<th>18 European countries</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1958/59 to 1960/61</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commodities not at risk</td>
<td>32</td>
<td>80</td>
<td>56</td>
<td>68</td>
<td>52</td>
<td></td>
</tr>
<tr>
<td>Commodities at risk</td>
<td>66</td>
<td>17</td>
<td>39</td>
<td>32</td>
<td>46</td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>2</td>
<td>3</td>
<td>5</td>
<td>-</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td></td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

To complete the perspective it may also be noted that total exports to the 18 European countries in question represented nearly 47 per cent of Australian exports in the period in question. This percentage was declining over the period - from 51 per cent in 1958/59 to 42 per cent in 1960/61.

The following are some of the main commodities comprised in the foodstuffs and metals groups, the detail of which enables a clear picture to be obtained of the group of exports considered at risk:
Australia. Exports of selected commodities
-average 1958/59 to 1960/61
£A millions per annum

<table>
<thead>
<tr>
<th>Total</th>
<th>Britain</th>
<th>Six</th>
<th>Seven</th>
<th>Peripherals</th>
<th>Other destinations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Butter</td>
<td>24.4</td>
<td>19.8</td>
<td>1.2</td>
<td>-</td>
<td>3.4</td>
</tr>
<tr>
<td>Cheese</td>
<td>4.7</td>
<td>3.2</td>
<td>0.1</td>
<td>-</td>
<td>1.4</td>
</tr>
<tr>
<td>Eggs</td>
<td>2.7</td>
<td>2.0</td>
<td>0.3</td>
<td>-</td>
<td>0.4</td>
</tr>
<tr>
<td>Fish</td>
<td>4.1</td>
<td>-</td>
<td>0.1</td>
<td>0.1</td>
<td>4.0</td>
</tr>
<tr>
<td>Honey</td>
<td>0.6</td>
<td>0.6</td>
<td>-</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Meat</td>
<td>70.3</td>
<td>32.0</td>
<td>1.2</td>
<td>0.1</td>
<td>36.7</td>
</tr>
<tr>
<td>Canned meat</td>
<td>12.7</td>
<td>8.7</td>
<td>0.2</td>
<td>-</td>
<td>3.8</td>
</tr>
<tr>
<td>Meat extracts</td>
<td>0.7</td>
<td>0.3</td>
<td>0.2</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Milk</td>
<td>10.1</td>
<td>1.3</td>
<td>0.1</td>
<td>-</td>
<td>8.7</td>
</tr>
<tr>
<td>Fruit</td>
<td>9.7</td>
<td>5.3</td>
<td>0.9</td>
<td>1.4</td>
<td>2.1</td>
</tr>
<tr>
<td>Dried fruit</td>
<td>10.3</td>
<td>5.4</td>
<td>0.6</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Canned fruit</td>
<td>11.7</td>
<td>10.4</td>
<td>0.1</td>
<td>0.1</td>
<td>1.1</td>
</tr>
<tr>
<td>Cereals</td>
<td>89.8</td>
<td>20.0</td>
<td>17.5</td>
<td>0.8</td>
<td>49.5</td>
</tr>
<tr>
<td>Prepared grain</td>
<td>21.5</td>
<td>2.1</td>
<td>-</td>
<td>-</td>
<td>19.4</td>
</tr>
<tr>
<td>Sugar</td>
<td>31.4</td>
<td>16.2</td>
<td>-</td>
<td>-</td>
<td>15.2</td>
</tr>
<tr>
<td>Lead</td>
<td>17.2</td>
<td>11.2</td>
<td>0.2</td>
<td>0.1</td>
<td>5.7</td>
</tr>
<tr>
<td>Zinc</td>
<td>3.9</td>
<td>0.7</td>
<td>-</td>
<td>-</td>
<td>3.2</td>
</tr>
<tr>
<td>Copper</td>
<td>7.7</td>
<td>0.3</td>
<td>1.7</td>
<td>-</td>
<td>5.6</td>
</tr>
<tr>
<td>Iron and steel</td>
<td>28.0</td>
<td>0.6</td>
<td>0.4</td>
<td>-</td>
<td>27.0</td>
</tr>
</tbody>
</table>

SOURCE: Overseas Trade Bulletin (calculated).

The commodities at risk will be considered first in the context of the formation of the Community of the Six, secondly in relation to the Free Trade Association and thirdly on the assumption of British entry into the Community; finally some notes on the significance of association of other European countries with the Community. It will be noted that the commodities at risk in connection with the union of the Six are the same as those at risk if Britain is associated but that the problem is intensified greatly by British association.
because of the wider range of exports in which a significant volume of trade is involved being affected by British association and the loss of the current preferential position on the British market. The Free Trade Association, it is noted, currently presents little threat to Australia's trade. The association of the continental members of this Association and of the peripherals with the Six will it is noted involve risk of a small trade loss and will in addition greatly increase the agricultural productive capacity of the Community. The fact that Greece is already associated will be taken account of also when discussing the effect of the existing Community.

The existing Community

On the basis of the figures for the three years considered above, the amount of Australian export trade at risk by reason of the formation of the existing Community is about £27\(\frac{1}{2}\) millions. This comprises mainly foodstuffs, the largest component of which is cereals, £17\(\frac{1}{2}\) millions. The G.A.T.T. Secretariat has estimated that net imports of foodstuffs, other than tropical beverages, of the Six in 1973/75 are likely to be nil; any imports, say of hard wheat from Canada, being balanced in value by exports of other foodstuffs.\(^{(5)}\)

Cereal production of the Community is expanding, notably in France, and the preferential treatment which the common agricultural policy, recently initiated, accords and will increasingly accord to French production, will encourage a further measure of expansion. Besides expansion in wheat

\(^{(5)}\) G.A.T.T., op. cit., pages 28 and 35.
production French policy is also directed to the expansion of production of coarse grains, such as barley. It is probable that Australia will lose its trade with the Six as the evolution of the Community proceeds. The E.E.C. estimates that wheat imports will virtually disappear by 1965 and coarse grains imports, on its median assumption, will decrease by about 17 per cent by that time. In 1959/60 the Community was 94.1 per cent self-sufficient in wheat and 78.1 per cent self-sufficient in coarse grains. (6) At present Australia exports wheat to Germany and coarse grains (barley and oats) to all countries of the Community except France.

Butter, which Australia now exports to all members of the Six except the Benelux countries, will be supplied in future by the Netherlands. The Community, in fact, plans to turn from being a small net importer to a heavy net exporter by 1965.(6)

The question of future meat exports to the Six is more controversial. At one stage it appeared that the considerable increase in consumption that could be anticipated by reason of growth of personal incomes in the Community would lead to an increase in net imports, particularly of beef. (7) However, more recently it has become apparent that the Six are planning substantial increases in production. They have in fact estimated (on the median of three assumptions) that their beef import will decrease somewhat by 1965. (6) Increase of meat production is now regarded in the Community as being a possible solution to their farm problem; that is to raise

the standards of living of persons engaged in agriculture

-165-
towards that of other sectors of the Community whilst avoiding

-165-
a drastic denudation of the farm population. Intensive use

-165-
of small farms for cattle raising may involve less adjustment

-165-
than the creation of efficient agricultural units. On the

-165-
other hand the increasing productivity of the French cereal
growing areas does not permit of any conclusion to be reached

-165-
that increased meat production will lead to decreased cereal

-165-
production. The industries are in fact to some extent

-165-
complementary. Production of eggs in the Community is also

-165-
likely to increase substantially.

The trade in dried fruit is likely to disappear as a
result of the association of Greece with the Community and the
consequent preference given to imports from that source. Some
trade in fresh fruit, mainly apples and pears may remain,
because of the seasonal factor. Australian fruit arrives in
April to July and currently fills in a gap in the availability
of local production. However, the improved use of cold storage
facilities and the preference given to member states, may result
in Community production increasingly supplying these marginal
needs. It is significant that Australia exports no fruit to
the main producing country, Italy.

In regard to metals the market for lead, zinc and
aluminium in the Six will be reduced because of the protection
given to local smelting and the heavy increase in production
developing in the associated countries. Australia is only a
small exporter of lead to the Six. Zinc is exported at present
in mineral form, as has been noted above. Aluminium is not yet an Australian export but large exportable surpluses are expected in future years. The small trade in iron and steel has survived despite the fact that the Coal and Steel Community is fully in operation. Trade in copper is not yet threatened but the possible association of territories such as the Rhodesias could alter the position.

Potential exports of coffee, coconut products and timber from New Guinea to the Six are likely to suffer because of the preferential position given to the associated countries. New Guinea exports coffee to the Six and will need to increase exports to destinations other than Australia.

In the absence of integration there was some prospect of improving trade in these commodities to some extent but in the circumstances it may well be that some £27½ millions of trade is lost. A loss of this magnitude could be made up by increase in demand for wool but it is by no means certain that integration will have the effect of promoting such an increase. Moreover, Australia's economic stability will lessen to the extent that she becomes more dependent on exports of one commodity.

Australia's small but by no means negligible trade with New Caledonia and other associated territories of the Six appears already to be suffering by diversion of trade to the Six through tariff and licensing preferences. Unless the discrimination becomes very acute a fair volume of trade should, however, remain because of Australia's favourable geographical position as a supplier to these markets.
The association of Britain, the Scandinavian countries, Austria, Switzerland and Portugal provides for free trade in industrial products. Australia has only a small export trade in industrial products with these countries, the most significant market being Britain. It is possible, for example, that Australia's trade in leather could be affected by reason of free entry being accorded leather from the associated countries. The same applies to a large variety of miscellaneous manufactured goods (annual trade £3 to £4 millions) whose market in Britain depends largely on the preferences received. Probably, in either case, the loss of trade would only be marginal.

Related to the association agreement are certain agreements on agricultural trade made for the benefit of Denmark. Insofar as Britain is concerned the products covered are insignificant in the export trade of Australia. So far as other members of the association are concerned Australia's export trade in the items covered by the agreements is small and unlikely to be much affected.

Any adverse effect on Australia's export trade arising from the creation of the Association should be counterbalanced by the support given to the British economy through the assurance of markets for British goods in the countries concerned. A healthy British economy is important to maintain import demand for Australian products.
British membership of the Community

If Britain succeeds in entering the Community it appears that after a short transitional period, probably lasting until the end of 1969, Australia will lose its existing preferential advantages in Britain.

These advantages include long-term agreements of meat and sugar assuring a market at remunerative prices, an assurance of purchase of 750,000 tons per annum of wheat, substantial tariff preferences on beef, canned meats and extracts, canned fruits, cheese, eggs not in shell, flour, barley, fodder grains, sugar, milk, raisins, soups, jams, gelatine, tallow and other fats, leather, timber, wine and manufactures and minor preferences on rice, oats, currants, butter, apples, pears and dried peas. Moreover, the duty free entry which is received on all but a very few goods, will be lost. Instead of this free and preferential entry Australia will be faced with external barriers having the effect that Community products and products from the associated countries and territories, including European associates, will find a market in preference to production of countries outside the area.

The production possibilities of the expanded Community are such that overall there will be no need to import wheat and in fact so far as soft wheat is concerned, and this is the type of wheat predominantly exported by Australia, the Community will be an exporter. There may still be some demand for fodder grains, despite increased production, if the livestock industry expands. So far as can be seen at present the system followed by the Community in regard to (7A) The preference on butter has been suspended during the duration of a quantitative arrangement now in force. The effect of the suspension is not to affect Australian
imports is likely to depress world prices for grains. The decreased market for outside suppliers will accentuate these effects. The loss of preference on, say, barley in Britain will tend to depress Australian returns if indeed it is possible to make any sales in the competitive conditions likely to arise. British membership of the Community will therefore it appears, seriously affect Australia's grain exports. Although in recent years substantial sales of wheat have been made by Australia to China, this is not a market which can with confidence be expected to endure. The loss of the British market, together with that of the Six would deprive Australia of an important proportion of its regular markets for unprepared grains. As the market for prepared grains in other parts of the world is very competitive and may meet increased competition from Community exports, a severe curtailment of grain production may become necessary unless some new solution is found.

It has already been noted that there are possibilities for substantial increase in beef consumption in the Six but that these may be balanced by increased production. The Six produced 91\(\frac{1}{2}\) per cent of their requirements of beef in 1959/60 and if Britain, Denmark, Norway and Ireland were added the degree of self-sufficiency would have been 93.6 per cent.(6) Due to the rise in consumer prices which will take place in Britain on the adoption of the common policy for beef there appears little likelihood of expanded consumption in that country. In the circumstances no confidence can be
felt that Britain will continue to be a substantial importer from outside the Community. Even if Britain does continue to import from outside sources the Australian position will be worsened by the loss of preferences that amount to 20 per cent in the case of some types of beef and canned beef. The Australian trade has been developed since the 1932 Ottawa Agreement by means of regulation of imports of foreign meat by Britain now replaced by the guarantees under the Meat Agreement; preferences on beef were also introduced later in the 1930's. In a condition of competitive equality with their shorter sea haul and consequent greater ease to supply the more palatable chilled beef rather than the frozen beef mostly supplied by Australia, what market there is may be taken by the South American countries. Argentina is even in present conditions a much more important supplier of beef to the British market than is Australia. These countries may also capture the market for lamb and mutton; New Zealand also appears to have some advantage over Australia in this trade. No preferences are enjoyed on lamb and mutton but a market is assured by the Meat Agreement. The loss of the meat and canned meats trade would be very serious for Australia as can be seen from the figures. If a substantial market for lower grade beef had not developed in the United States in recent years the outlook would be worse. The United States market could, however, be restricted on account of farm politics at any time and in addition Australia's position in this market is due to the fact that Argentinian beef is excluded on account of foot and mouth disease.
which is not present in Australia. In other words Australian
beef could be excluded from the United States at any time if
this disease broke out in Australia. On the other hand the
British market for Australian beef has been a steady and
reliable one and its loss would leave the Australian industry
in a precarious position. This industry is of major importance
to the tropical areas of Australia.

The Community's plans for expansion of production of
dairy products will ensure that there will be no need for
Britain to import from outside countries. Some limited demand
for cheddar cheese may persist although this may disappear
as continental cheeses become available or the Community's
production is adapted to British taste. When membership of
Denmark and Ireland is also taken into account, it appears
likely that the enlarged Community may be a net exporter, if
indeed export markets exist. At present Britain is the only
really substantial market in the world for butter. There is
a demand for processed milks, notably from Asia, though much
of this is supplied under aid plans. The dairying industry
in Australia receives government subsidies and generally export
prices are well below those paid by the Australian consumer.
The loss of the British export market would therefore not
be without its compensations if it were possible to sub-
stitute for dairying some other form of intensive husbandry
providing export income but the export outlook in general
does not suggest that this can be the case. The dairying
areas affected could include some specialised districts,
such as the north of Tasmania, which could as a result become denuded of population.

The British market for eggs has not been a large one in recent years due to heavy expansion of subsidised production. Such market as there is will be supplied from Community sources under the common agricultural policy.

Canned fruit export to Britain will, it is considered, virtually disappear as a result of the loss of preferences. Australia has in general been unable to enter non-preferential markets against United States competition. The market for dried fruits in Britain is also vulnerable because of the association of Greece with the Community, the likely association of Turkey on similar terms and the loss of preferences vis-a-vis the United States and the Middle East countries. The trade figures show that over half Australia's export trade in dried fruits is at risk and over 90 per cent in the case of canned fruits. Fruit growing areas, including those under irrigation schemes, may be badly affected.

The market for fresh fruit in Britain will be affected for the reasons mentioned when the market in some members of the Six was considered. The loss of preferences in relation to South American countries will also affect the remaining seasonal market. The system of grading fruit in the Community may present difficulties as Australian fruit will have to conform to exacting and new standards.

It has already been noted that the Six are planning an exportable surplus of sugar and that Australia is likely to
lose its guaranteed market in Britain under the Commonwealth Sugar Agreement and in addition substantial tariff preferences. The future market for Australian sugar in Britain must be considered in doubt.

The timber trade is likely to be affected by loss of preferences and inclusion of tropical areas in the Community.

The conditions underlying the market in Britain for metals would be similar to that discussed in the case of the Six. It is likely to prove difficult to market lead, zinc, aluminium and possibly copper. The volume of trade is greater than in the case of the Six and loss of this trade would affect many outlying communities and development plans.

The useful and growing trade in manufactures will be affected by loss of preferences and subjection to the common tariff. Trade in leather is very vulnerable to continental competition. Other items likely to be seriously affected include tallow, whale oil and wines.

The prospects, as was noted in the case of the Six, are not unfavourable for wool, minerals and hides and skins. These items represent under one third of Australian exports to Britain in the period for which figures have been extracted. The total trade vulnerable is in the region of £150 millions per annum in the case of Britain. This rises to £184 millions per annum when trade with the Six and other countries likely to be associated with the Community is considered.

A more optimistic appraisal of Commonwealth and Australian prospects was given by the Economist Intelligence Unit in 1960.
The following quotations are from its publication "The Commonwealth and Europe":

"Britain would take part in the policy making of the whole group and would therefore throw its weight on the side of the policies which would benefit Commonwealth trade. Thus Britain could press for lower tariffs and larger quotas on imports of those manufactures which the Commonwealth supplies and for lower European price levels and hence higher imports of agricultural produce." (8)

"The United Kingdom could therefore accept a common (agricultural) policy provided that it was sufficiently liberal and as a safeguard the United Kingdom might have the right either to cut off imports from the continent or to allow free entry from the Commonwealth, should Europe's imports from the Commonwealth fall below agreed levels." (9)

"The best policy (for temperate foods) would be to barter free entry into the United Kingdom in exchange for a very liberal import policy for the whole of Europe. There would be a gradual changeover to a European tariff which would have to be low on all products of importance to the Commonwealth and if total European imports of such products from the Commonwealth were to decline as a result of the new system there should be escape clauses for the United Kingdom to invoke, safeguards in the form of tariff-free quotas for United Kingdom imports of Commonwealth manufactures and for temperate foodstuffs either tariff-free quotas or perhaps ..."

measures to restrict imports from the Continent." (10)

Although no doubt, as the Unit concludes, British association with Europe in the field of agriculture may have some tendency to promote lower prices and thus greater consumption, it must not be overlooked that Britain followed a policy of protecting agriculture almost as comprehensive as that of the Six. Production of cereals, meat, eggs, sugar and dairy products have all expanded since the 1930's. (11) The fact that Britain continues to remain the major importer in the world of most foodstuffs is attributable to a shortage of land as well as to her low-price policy. Any general move towards diminution of protection as a result of British association with the Community would not therefore follow automatically. Even in relation to free entry the British policy can be ascribed to the 1932 Ottawa Agreement rather than to a deliberate decision of post-war governments who have found the burden of production subsidies a heavy one and might have welcomed the chance to ease this by means of a protective tariff.

Apart from the interests of Britain, it has however become apparent since the date of the Unit's publication that there is no immediate likelihood of a liberal entry policy for the whole of Europe nor is there any prospect of Britain being allowed to retain safeguards to ensure imports from the "old Commonwealth" do not decrease. In fact the concept of duty-free quotas is on the way out in the Community.

(10) E.I.U., op. cit. page 469. (11) Production of wheat and barley and of dried milk stood in 1958 at 228 per cent of pre-war levels, of cheese at 200 per cent, sugar and eggs 183 per cent and beef and pork 143 per cent. There was a small increase in oats production and a very small decline in butter, condensed milk and mutton.
In regard to metals the Unit states "Free entry of lead and zinc into the United Kingdom from the Commonwealth combined with an origin procedure could hardly threaten the continental smelters". (12) "Tariff free entry of aluminium into the United Kingdom for the Commonwealth should be possible." (13)

It is realistic to assume that the Six will want to continue to protect their smelting industry; there are also industries in some of the possible European associates (e.g. aluminium in Norway) and important developments in associated African countries. The further assumption that there will be no desire to take over the British market for these suppliers is more difficult. The reasoning appears defective in assuming that an origin procedure would solve the objections of the Six to free entry into Britain; the Carli Plan developed during the Free Trade Area discussions showed that the Six were very concerned that free entry in these circumstances would distort competition, and that it was not merely re-export of the imported goods that concerned them. The Six would therefore be unlikely to allow free entry for Britain unless there was in fact free entry into the Community as a whole which appears an unlikely possibility.

The same optimism permeates the specific judgments of the Unit in viewing the specific position of Australia: "Australia's growth prospects are much less dependent (than New Zealand's) on Europe's trading arrangements. Good access for foodstuffs is, nevertheless, a significant factor. Australia with its bigger home market is also better able to

(12) E.I.U. op.cit. page 464  (13) E.I.U. op.cit. page 465  
(14) E.I.U. op.cit. page 471.
generate its own industrial growth and to attract foreign
capital. All three countries (Australia, Canada, New Zealand)
give the United Kingdom substantial preferences which could,
if necessary, be used by them in bargaining with the Six.
Since Australia and Canada are big and growing markets they
are in a particularly strong position. They might also, in
order to secure a share in the expanding European market for
foodstuffs and in Canada's case for manufactures too, consider
applying for formal association with the new European economic
group. The removal of protection for their industries would
go against the current trend but they should be as well able
to contemplate this over an extended transitional period as
the poorer European countries such as Greece, Portugal and
Turkey, which are already doing so."

There is no doubt that New Zealand's dependence and
vulnerability is even greater than that of Australia if only
because wool plays a less important part in the exports of
the former country. Australia's ability to grow and to attract
capital is, however, dependent on a satisfactory export
income. There is no indication that the Six are prepared to
give substantial advantages in exchange for elimination of
British preferences in Australia; in fact it is obvious that
these will die a natural death if Australia's preferences in
Britain go. The G.A.T.T., strongly backed by the United States,
prevents the Six sharing these preferences with Britain. The
possibility of Australian association with the Community is
considered at length in a later chapter. It may here be noted,
(14) E.I.U., op. cit. page 471.
however, that it appears that the Six would not be interested in this.

The opinion may also be expressed that Australia and Canada are no more likely to secure satisfactory access for foodstuffs to the Six because of their importance as a market than Canada has been able to secure satisfactory access to the United States market for foodstuffs which means very little access indeed. Despite one or two assumptions that can be criticised as over-optimistic much of what the Unit said was reasonable in 1960 and has only been falsified by the event. It would not have been considered possible in 1960 that Britain would have considered entering the Community on the terms which have lately been mooted.

Before leaving the subject of the vulnerability of Australian exports to the enlarged Community it should be noted that there has been some talk of world-wide commodity arrangements as a solution to these problems.

The suggestion that such arrangements might be concluded appears to have been put on the map by the French Minister of Finance, M. Baumgartner, who mentioned the idea in a speech to the G.A.T.T. in November, 1961. It was apparently envisaged that industrial countries would pay for their imports of agricultural products a higher price than at present, comparable to the price guaranteed to their own farmers. Surpluses of all producing countries would be

(15) Exports of Canada to the U.S. in 1959 of $3727 m. included foodstuffs and beverages of $301 m. or 8 per cent. Principal components were fruits, whisky, vegetables and fish. U.S. Department of Commerce statistics. Canadian wheat is virtually banned.
disposed of to underdeveloped countries at concessional prices. This would require the creation of a fund to subsidise the concessional sales. The scheme would be accompanied by production restrictions in view of the fact that higher prices might stimulate production. (16)

If the Community maintains its agricultural plans, and it is difficult to see it doing otherwise, (17) the concept of higher import prices will be of little meaning as there will be few imports. If so the only benefit Australia would be likely to receive from the scheme would arise if industrial countries were willing to subsidise Australian exports to the under-developed countries, a concept that seems too good to be true. Restrictions on Australian production might not be acceptable unless the level of production were generous. Schemes of this nature appear most suitable for commodities which have been in recent years the subject of disposal programmes to the under-developed countries, such as cereals and processed milk.

The Baumgartner scheme does not appear to have been embraced by Commonwealth Prime Ministers at their September, 1962 London conference. In the Conference communique there is reference, for instance, to disposal of surpluses to needy peoples to the fullest extent compatible with the interests of traditional suppliers. This is a formula more suitable for

(17) Professor Lewis regards the Plan as an attempt to stave off agricultural adjustment in the E.E.C. op.cit. page 143.
the traditional method of surplus disposal rather than for
the Baumgartner method. The fact that Prime Ministers had no
particular solution appears from the statement in the communique
that they would join in "comprehensive international efforts
by all available means to expand trade in ....primary
products...."(18).

Association of other European countries

The association of the "Seven" and the "Peripherals"
declared earlier in this chapter and whose imports from
Australia are there set out, will also affect some of this
trade. It will be noted that this trade is small and mainly
in vegetable foodstuffs. These include apples and pears to
Scandinavian countries, coarse grains to Denmark and wheat to
Spain. It has already been noted that imports of these
commodities into the Community will be affected by integration.

However, the more important implication of association
of these countries with the Community is their capacity to
export agricultural produce. Their inclusion in the common
agricultural policy will make it even more certain than at
present that the Community will import little in the way of
foodstuffs and may generate substantial surpluses. Some of
the more important exports are grains from Turkey, Ireland and
Sweden; dairy products and meat from Ireland, Denmark, Sweden
and Finland; dried fruits from Spain, Greece and Turkey;
canned fruits from Spain and wines from Spain and Portugal.
Although much of the meat exported is pigmeat, beef is also
important; Ireland exports live cattle.

(18) Paragraph 10.
If associated with the Community these countries will, to some extent, step into the privileged position vacated by the Commonwealth in the British market.

(ii) Imports

Australia - imports - average 1958/59 to 1960/61 £A millions per annum

<table>
<thead>
<tr>
<th></th>
<th>Total</th>
<th>Britain</th>
<th>Six</th>
<th>Seven</th>
<th>Peripherals</th>
<th>Other sources</th>
</tr>
</thead>
<tbody>
<tr>
<td>Animal and vegetable</td>
<td>82.1</td>
<td>8.4</td>
<td>4.6</td>
<td>2.8</td>
<td>0.8</td>
<td>65.5</td>
</tr>
<tr>
<td>substances</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yarns, Textiles, Apparel</td>
<td>113.5</td>
<td>38.0</td>
<td>16.2</td>
<td>4.8</td>
<td>0.3</td>
<td>54.2</td>
</tr>
<tr>
<td>Paints, etc.</td>
<td>6.7</td>
<td>3.7</td>
<td>1.0</td>
<td>0.5</td>
<td>0.1</td>
<td>1.4</td>
</tr>
<tr>
<td>Oils, fats, waxes</td>
<td>107.7</td>
<td>2.0</td>
<td>1.1</td>
<td>-</td>
<td>0.8</td>
<td>103.8</td>
</tr>
<tr>
<td>Minerals</td>
<td>7.9</td>
<td>0.7</td>
<td>0.4</td>
<td>0.5</td>
<td>0.1</td>
<td>6.2</td>
</tr>
<tr>
<td>Metals and semi-manufactures</td>
<td>48.1</td>
<td>20.0</td>
<td>5.1</td>
<td>1.4</td>
<td>0.2</td>
<td>21.4</td>
</tr>
<tr>
<td>Vehicles</td>
<td>85.2</td>
<td>49.6</td>
<td>16.8</td>
<td>0.3</td>
<td>-</td>
<td>18.5</td>
</tr>
<tr>
<td>Aircraft</td>
<td>17.3</td>
<td>4.8</td>
<td>2.4</td>
<td>-</td>
<td>-</td>
<td>10.1</td>
</tr>
<tr>
<td>Metal manufactures</td>
<td>27.8</td>
<td>16.7</td>
<td>3.3</td>
<td>0.9</td>
<td>-</td>
<td>6.9</td>
</tr>
<tr>
<td>Electrical machinery</td>
<td>42.9</td>
<td>24.0</td>
<td>7.2</td>
<td>2.5</td>
<td>-</td>
<td>9.2</td>
</tr>
<tr>
<td>Other machinery</td>
<td>140.2</td>
<td>68.2</td>
<td>18.0</td>
<td>7.0</td>
<td>0.1</td>
<td>46.9</td>
</tr>
<tr>
<td>Rubber &amp; mfrs.</td>
<td>21.5</td>
<td>2.7</td>
<td>0.8</td>
<td>0.1</td>
<td>-</td>
<td>17.9</td>
</tr>
<tr>
<td>Timber</td>
<td>20.0</td>
<td>0.4</td>
<td>0.4</td>
<td>1.4</td>
<td>-</td>
<td>17.8</td>
</tr>
<tr>
<td>Earthenware, etc.</td>
<td>17.3</td>
<td>8.5</td>
<td>3.7</td>
<td>0.7</td>
<td>0.1</td>
<td>4.3</td>
</tr>
<tr>
<td>Pulp, Paper, Board</td>
<td>42.4</td>
<td>10.5</td>
<td>1.8</td>
<td>11.4</td>
<td>-</td>
<td>18.7</td>
</tr>
<tr>
<td>Stationery, etc.</td>
<td>15.4</td>
<td>10.3</td>
<td>1.3</td>
<td>0.3</td>
<td>-</td>
<td>3.5</td>
</tr>
<tr>
<td>Sporting goods, etc.</td>
<td>10.8</td>
<td>3.0</td>
<td>2.2</td>
<td>1.9</td>
<td>-</td>
<td>3.7</td>
</tr>
<tr>
<td>Optical, etc.</td>
<td>15.1</td>
<td>5.7</td>
<td>3.5</td>
<td>0.7</td>
<td>-</td>
<td>5.2</td>
</tr>
<tr>
<td>Chemicals</td>
<td>48.2</td>
<td>20.6</td>
<td>9.1</td>
<td>3.1</td>
<td>0.1</td>
<td>15.3</td>
</tr>
<tr>
<td>Plastics</td>
<td>11.8</td>
<td>4.9</td>
<td>1.9</td>
<td>0.2</td>
<td>-</td>
<td>4.8</td>
</tr>
<tr>
<td>Ships</td>
<td>3.0</td>
<td>2.8</td>
<td>-</td>
<td>0.1</td>
<td>-</td>
<td>0.1</td>
</tr>
<tr>
<td>Miscellaneous (a)</td>
<td>38.5</td>
<td>18.4</td>
<td>4.4</td>
<td>0.4</td>
<td>-</td>
<td>15.3</td>
</tr>
<tr>
<td>Total (b)</td>
<td>923.4</td>
<td>323.9</td>
<td>105.2</td>
<td>41.0</td>
<td>2.6</td>
<td>450.7</td>
</tr>
</tbody>
</table>

NOTES: (a) includes outside packages
(b) excludes non-commercial items and gold

SOURCE: Oversea Trade Bulletin (calculated).
It will be noted that in the period under review exports averaged £406.4 millions per annum to the eighteen countries in question and imports averaged £472.7 million. Australia also experienced considerable net outgoings with the area for freight and insurance.

Integration in Europe can affect Australian imports in a number of ways. If integration leads to lower costs, lower prices may be offered in the Australian market. On the other hand if inflation in the Community leads to higher costs or if monopoly develops, this may lead to higher prices being offered in the Australian market. A downwards movement in prices should lead to the Community securing a greater share of the Australian market, an upward movement to a smaller share.

If the Community engages in extensive tariff bargaining with the United States, the lower tariffs will lead to greater competition and thus to lower prices. These countries together should then increase their share of the Australian market which is, however, already considerable.

There does not appear to be much scope for monopoly influences, coming into being by reason of European integration, to raise the level of export prices to Australia. According to the above table Europe is only predominant as a supplier of paints and ships and there appear to be alternative sources of supply available for these goods. Examination of detailed import statistics does not change the picture. Except for a few minor items such as certain types
of stationery, European suppliers do not monopolise the Australian market. In 1958/9 certain chemicals such as potassium compounds, styrene and toluol were supplied exclusively from a number of European countries but the removal of dollar licensing has brought North America into the market. There are still a number of items of which, because of large preferences, Britain is the only substantial supplier. Integration would only be likely to lead to monopolistic developments if the only potential suppliers were from Europe. In most if not all cases there should be ample competition from North America and Japan.

So far as the Free Trade Association is concerned there should be no effect on imports as a result of integration. It is true that a large proportion of timber imports come from Scandinavia but the scope for concerted price raising should be small if any. In particular an increasing amount of Australian timber imports is coming from New Zealand.

British association has already been mentioned in connection with possible monopoly influences. The most important effect of British association on Australian imports is likely to be the loss of preferences in the Australian market. This should lead to more competitive buying by Australian importers and a general lowering of import prices. A substantial amount of trade may be diverted away from Britain. Some of this will accrue to the Six but the United States and Japan should also benefit.
(c) **Terms of Trade**

Viner points out that a tariff-levying country may be able to obtain economic benefits which may be able to be exploited more effectively combined in customs union than if it operates as a separate tariff area. The benefit to the customs area carries with it corresponding detriment to the outside world. The tariff not only diverts demand from foreign goods to domestic goods but also alters in favour of the tariff-levying country the rate at which its exports exchange for the imports still surviving the tariff. The greater the economic area of the tariff-leving unit, the greater is likely to be the improvement in its terms of trade with the outside world resulting from the tariff. This is because its elasticity of demand for imports is likely to increase with size whilst the foreign elasticity of demand for its exports is likely to decrease. (19) Moreover, the greater the size of the unit, the more effective bargaining power it possesses. (20)

The formation of the Community, it has already been noted, is likely to reduce world demand for foodstuffs and the system of treating imports, particularly in the case of cereals, is also likely to depress prices. The general level of world prices for foodstuffs may therefore fall due to excess of supply over demand. There is a possibility of higher prices prevailing if the world-wide agreements suggested by France eventuate but it has been considered earlier that

(20) J. Viner, *op. cit.* page 56.
it is rather optimistic to expect Australia to receive substantial benefits under these agreements. It is therefore to be expected that the effect of European integration will be to depress Australian export prices of foodstuffs. This may also happen in regard to metals whilst the position in regard to wool is indeterminate.

On the import side, however, the conclusion has been that Australian import prices should not rise but may well fall, particularly due to the elimination of British preferences. Falling import prices may necessitate rising tariffs but the net cost to the Australian economy is reduced.

The effect on Australia's terms of trade depends on the relationship between two falling sets of prices. The fall in export prices is of course the more important of the two and unless substantial markets can be secured elsewhere full advantage of falling import prices cannot be obtained. During past years there has been a steady tendency for commodity prices to fall in relation to the prices of manufactured goods. The formation of the Community appears likely to accentuate this tendency which may continue after the once for all benefit of reduced prices due to elimination of import preferences on manufactures has been exhausted.

Overall the outlook for Australia's terms of trade resulting from European integration is not favourable but it is overshadowed by the quantitative effects on trade likely to result.
Chapter 8  E.E.C. and E.F.T.A. - Effects on Australia

(b) Other aspects

(i) Balance of Payments

The Australian Balance of Payments for the three years ended June 1962 has been recorded as possessing the following features:

<table>
<thead>
<tr>
<th>£A millions</th>
<th>1959/60</th>
<th>1960/61</th>
<th>1961/2 Preliminary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports, f.o.b.</td>
<td>937</td>
<td>936</td>
<td>1080</td>
</tr>
<tr>
<td>Imports, f.o.b.</td>
<td>916</td>
<td>1046</td>
<td>859</td>
</tr>
<tr>
<td>Net outgoings - Transport</td>
<td>62</td>
<td>76</td>
<td>52</td>
</tr>
<tr>
<td>Travel</td>
<td>26</td>
<td>28</td>
<td>25</td>
</tr>
<tr>
<td>Investment Income</td>
<td>125</td>
<td>123</td>
<td>118</td>
</tr>
<tr>
<td>Government</td>
<td>22</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>Other</td>
<td>10</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1162</strong></td>
<td><strong>1305</strong></td>
<td><strong>1088</strong></td>
</tr>
<tr>
<td>Balance on current account</td>
<td>-224</td>
<td>-369</td>
<td>-8</td>
</tr>
<tr>
<td>Capital items:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inflow - official</td>
<td>40</td>
<td>3</td>
<td>5</td>
</tr>
<tr>
<td>private</td>
<td>183</td>
<td>225</td>
<td>92</td>
</tr>
<tr>
<td>balance</td>
<td>8</td>
<td>102</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>231</td>
<td>330</td>
<td>97</td>
</tr>
<tr>
<td>Monetary movements - increase</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>in reserves</td>
<td>7</td>
<td>-</td>
<td>89</td>
</tr>
<tr>
<td>- decrease</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>in reserves</td>
<td>-</td>
<td>39</td>
<td>-</td>
</tr>
</tbody>
</table>

Examination of trade prospects in the previous chapter indicated some possibility of saving on import prices. If this is assumed to be 7\(\frac{1}{2}\) per cent on imports from Britain (1961-62 £263.4 millions), the saving would be about 20 millions per annum. 7\(\frac{1}{2}\) per cent is below the average preference on all imports from Britain but it cannot be assumed that in all cases British goods are dearer than alternative supplies by the full preference margin so that the full preference would be saved by Australia when the preferences were removed.

On the export side it has been seen that about £184 millions of trade per annum could be lost if Britain and the other countries under consideration joined the Community. The total possible net loss of foreign earnings is therefore about £164 millions per annum. If the Six continue with Greece associated but without any other countries adhering the prospective loss is about £27 millions per annum. No account has been taken in these figures of possible loss of trade to overseas territories such as New Caledonia and Rhodesia and Nyasaland.

It is apparent that unless extra markets can be found, losses of trade of the magnitude possible if Britain joins the Community will severely restrict Australia's ability to import. The position may be made more difficult still by the contraction of overseas investment in Australia.

If Australia became self-sufficient in oil some £75 millions of net imports per annum (1961/2 Imports £97.4 millions - Exports £22.4 Millions) could be saved.
This would, however, be less any remitted earnings of overseas companies engaged in extraction. Moreover, unless the price of local oil were no dearer than that of imported oil there would be some adverse reactions on the economy whose effect on the balance of payments might not be negligible.

(ii) Investment

The figures quoted above show the heavy dependence of Australia on overseas private investment. The make-up of overseas private investment in Australia in the years 1959/60 and 1960/61 was as follows:-

<table>
<thead>
<tr>
<th></th>
<th>1959/60</th>
<th>1960/61</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australian branches - unremitted profits</td>
<td>9.5</td>
<td>6.3</td>
</tr>
<tr>
<td>other investments</td>
<td>22.5</td>
<td>22.3</td>
</tr>
<tr>
<td>Australian subsidiaries - undistributed profits</td>
<td>59.2</td>
<td>56.9</td>
</tr>
<tr>
<td>other investments</td>
<td>68.8</td>
<td>160.0</td>
</tr>
<tr>
<td>Portfolio investment</td>
<td>32.8</td>
<td>47.9</td>
</tr>
</tbody>
</table>


Some idea of the countries of origin for this investment can be obtained from the following figures:-

Annual inflow of private investment to Australia from overseas countries by domicile of investor £A millions.

<table>
<thead>
<tr>
<th>Country</th>
<th>1959/60</th>
<th>1960/61</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>104.5</td>
<td>105.4</td>
</tr>
<tr>
<td>New Zealand</td>
<td>7.6</td>
<td>2.7</td>
</tr>
<tr>
<td>United States &amp; Canada</td>
<td>62.2</td>
<td>86.9</td>
</tr>
<tr>
<td>Other</td>
<td>16.2</td>
<td>34.7</td>
</tr>
<tr>
<td></td>
<td>190.5</td>
<td>229.7</td>
</tr>
</tbody>
</table>

Although figures for 1961/62 are not available, it appears likely, when the balance of payments figures are examined, that there was a severe falling off in investment into Australia in that year.

The formation of the Community and the association of Britain could both be expected to lead to increased investment in Europe by both British and American investors. "Moreover on present proposals it is difficult to see how sterling countries could be accorded", as they have been for many years, "more favourable access to British capital than Britain's partners in the Community - and indeed, there is a risk of which some Commonwealth governments are increasingly aware, that Britain might even be compelled to actually discriminate against sterling countries." (1)

Reasons for increased investment in Europe include the necessity for reorganising production and establishment of new plants and also the expected increase of profitability due to increased growth and possibly also due to some expectation of a measure of inflation. Moreover the prospects for profitable investment in Australia would be diminished by reason of the loss of market for primary products. The consequent precarious position of the balance of payments might also cause investors to re-evaluate the capital risks attendant on investment in Australia.

Although the figures for one year, 1961/2, are insufficient to enable a judgment to be made, it appears likely that these influences are already at work. Other influences have also been at work such as a decreased profitability of business in Australia, ascribed by many people to a cautious deflationary government policy. However, with export performances and prospects as they are, there is little choice in regard to the degree of internal expansion that can be reasonably undertaken. A further factor at present is the less healthy state of the United States balance of payments. Figures are not available to show whether United States investment in Australia has diminished but as this investment is very small from the United States point of view, if prospects of profitability were good this investment should not have been affected.

The order of magnitude of private investment in Australia, until very recently, has been comparable to that of net outgoings on invisible account and it has thus enabled Australia to strike an even balance when exports and imports are roughly the same. It should, however, be noted that the continued inflow of private investment has tended to increase the outflow of investment income (net outflow of investment income £83 millions in 1957/58; £125 millions in 1959/60)(2) There has, indeed, been a tendency, particularly in the case of American investment, for funds to be directed to highly

profitable consumption-creating industries and doubts have been expressed as to the utility of this investment to Australia. Overseas investment in "Commerce (including oil distribution and primary produce dealing)" increased from £3.6 millions per annum in 1956/57 to £43.2 millions in 1960/61, an increase more notable than that of "Vehicles, parts and accessories (including aircraft and ships)" which increased over the same period from £10.5 millions to £33.4 millions (2). Despite the misgivings expressed on this score it appears that maintenance of the flow of investment to Australia is beneficial. Certainly oil exploration would have been very slow without overseas capital investment.

European continental countries have not been important investors in Australia, this field being dominated by Britain and the United States. However, in due course, if the Community prospers, in view of the fact that the economies are mature, there should be ample funds for investment overseas.

The Rome Treaty requires some direction of investment within the Community. The European Social Fund (Chapter 2 of Title III) and the European Investment Bank (Title IV of Part Three) are examples in point. Moreover the Implementing Convention relating to associated countries and territories requires the provision of $581½ millions over the first period of five years (1958/62) in the countries and territories. Of this some $311½ millions provided by
other members of the Six was scheduled to be spent in the French territories and former territories. This latter sum would hardly have been directed in this manner in the absence of the Treaty. Rather larger sums are expected to be spent in the next five year period. In addition capital investment is to be undertaken in Greece.

When other members of the Six have a stake in the development of the former French territories this may well tend to increase of its own volition; in other words private investment will follow that of governments. This is based on the assumption that these associated countries will in fact find a ready and profitable market for their products in the Community; if they did not, they would hardly remain associated. In addition, private investment may be attracted into the associated countries from America and from Britain, whether or not the latter joins the Community.

Generally, therefore, whether or not Britain joins the Community, but particularly if she does join, some adverse effect, particularly in the early years, can be expected on overseas investment from most sources into Australia.

(iii) Development

Although Australia is a country with a relatively high standard of living there are great needs for development in order that the country can be fully utilised. An example of the type of development being undertaken in Australia is the Snowy River Schamm which has been undertaken by the Commonwealth and State governments and which will cost several hundreds of millions of £. This scheme provides
electric power, water for irrigation and flood control. An important example of private investment, to a large extent financed from overseas which is assisted by the Commonwealth Government, is oil exploration. Existing schemes only touch the fringe of developmental needs which remain acute in the northern part of the continent.

Before considering the likely effect of European integration on Australian development it will be of some value to set out some figures illustrating changes in the composition of Australian secondary production and imports over a period of twenty years.
### Percentage Composition of Production and Imports

<table>
<thead>
<tr>
<th>Factories</th>
<th>Value of Output</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Treatment of quarry products</td>
<td>2</td>
<td>2 1/2</td>
</tr>
<tr>
<td>Bricks, pottery, glass</td>
<td>2</td>
<td>1 1/2</td>
</tr>
<tr>
<td>Chemicals, paints/ etc</td>
<td>6</td>
<td>10 1/2</td>
</tr>
<tr>
<td>Motor and cycle</td>
<td>4</td>
<td>7 1/4</td>
</tr>
<tr>
<td>Smelting</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Engineering</td>
<td>3 1/2</td>
<td>7 1/3</td>
</tr>
<tr>
<td>Electrical</td>
<td>1 1/2</td>
<td>4</td>
</tr>
<tr>
<td>Wireless and amplifying</td>
<td>1 1/3</td>
<td>1 1/3</td>
</tr>
<tr>
<td>Other metals, machines</td>
<td>13 1/2</td>
<td>12</td>
</tr>
<tr>
<td>Precious metals, jewellery</td>
<td>1 1/2</td>
<td>1 1/2</td>
</tr>
<tr>
<td>Rubber</td>
<td>2 1/2</td>
<td>1 1/2</td>
</tr>
<tr>
<td>Skins and leather</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Textiles and textile goods</td>
<td>5 1/2</td>
<td>5</td>
</tr>
<tr>
<td>Clothing</td>
<td>7</td>
<td>5</td>
</tr>
<tr>
<td>Brewing</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Tobacco</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Mineral Waters</td>
<td>3 3/4</td>
<td>1 1/2</td>
</tr>
<tr>
<td>Food</td>
<td>26 3/4</td>
<td>17</td>
</tr>
<tr>
<td>Sawmills, joinery/ etc</td>
<td>4 1/2</td>
<td>4 1/2</td>
</tr>
<tr>
<td>Wood furniture, books</td>
<td>2</td>
<td>1 1/2</td>
</tr>
<tr>
<td>Paper, stationery</td>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>Musical instruments (small)</td>
<td>1</td>
<td>1 1/4</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>1</td>
<td>1 1/4</td>
</tr>
<tr>
<td></td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Sources:** Production—Commonwealth Bureau of Census and Statistics, Secondary Industries, 1938/39 and 1958/59.

**Imports—Overseas Trade Bulletins (excluding gold and silver)**

**Note:** because of the nature of the figures production statistics have been extracted as round numbers and fractions.
It may be noted that imports have increased eight times in value over the period whilst the value of production has increased under eight and one half times. Although these values are only indicative of the physical volume of trade, the general picture is one of stability in the relation between production and imports. With the relaxation of import licensing in 1959/60 the ratio should be even closer.

The composition of imports also exhibits considerable stability. Main increases are in petroleum and machinery whilst the main decreases are in textiles and apparel, food and drink and agricultural raw materials. On the production side main increases are in chemicals, engineering, vehicles and electrical goods whilst main decreases are in the food groups and also in clothing and brewing.

The changes in production appear well balanced. The expansion of the engineering group is in line with the increased demand in this sector evidenced by the heavy expansion of imports of machinery. It is also satisfactory that the increased production of vehicles has kept pace with demand. Decreased production of textiles, apparel and food are also in line with developments in the economy illustrated by the decreased importance of imports in these groups. The increase in import of petroleum cannot yet be paralleled in the production field but this development may not be far off. The figures only deal, however, with factory production and do not illustrate investment in services.
The above figures illustrate the importance of investment in the engineering and vehicles groups and the importance of adequate export income to enable maintenance of imports in the machinery and petroleum groups.

It is apparent that the prospects which has been outlined earlier in this chapter do not augur well for Australian development. Moreover existing development may well become unprofitable because of diminution in export demand. Particularly affected may be areas devoted to the production of vine fruits, the growing of apples, pears, peaches and apricots, fruit canning, the smelting of lead, dairying, grain production, sugar growing and crushing and cattle raising.

If export income lost in Europe is not made up in other directions the ability to import raw materials and machinery for manufacturing production will be impaired. (2A)

The amount of net income for trade at risk of £164 millions is about 16 percent of export earnings in a good year. It is, however, a relatively small proportion of Australia's gross national product of £7300 millions - about 2 percent. It would, however, be under-estimating the effect of loss of this income if it were considered that only 2 percent of national product was at risk. A considerable multiplier effect would attach to loss of export income of this nature. Some secondary effects of such a diminution of external income have already been noted; these include loss of foreign investment and shortage of essential goods
for industry. Government policy would need to be directed even more than at present to the need for conserving foreign exchange. Developmental projects directly or indirectly involving substantial imports would need to be reduced and personal consumption discouraged.

Under the stimulus of shortages, in the absence of governmental direction to the contrary, a number of new industries would spring up, many of which would be economically undesirable. In order to avoid unemployment these developments might have to be tolerated. Increases in standards of living would be checked and these standards might in fact fall.

(2A) It is assumed for the purpose of this study that a very high proportion of this income would be lost. Because of the variety of circumstances that could obtain, no reliable estimate can in fact be made of the magnitude of the loss and the subject has been the subject of political controversy in Australia. The assumption of a loss of a high proportion of this income can be justified by extrapolating from present trends and developments whilst the possibility of a much more favourable position obtaining rests on more speculative assumptions. Optimism can often be rewarded by unexpected results especially when accompanied by ingenuity and a will to succeed. But the view is taken for the purpose of this part of the study that the effects on Australia of European integration are those of a direct nature and that it is not possible to take into account all the circumstances which could have the effect of alleviating Australia's position, especially when many of these circumstances (such as the development of effective demand in other regions of the world) would have little if any connection with European integration.
for industry. Government policy would need to be directed even more than at present to the need for conserving financial resources. Developmental projects would be reduced to a minimum and personal consumption discouraged.

Under the stimulus of shortages, in the absence of governmental direction to the contrary, a number of new industries would spring up, many of which would be economically undesirable. In order to avoid unemployment these developments might have to be tolerated. The standard of living would fall.

Developments of this nature would tend to discourage migration which is essential for the continued acceleration of Australian development. The increase in unemployment in 1961, combined with increased prosperity and labour shortages in Europe, have already reduced migration to Australia. Net gain of settlers from immigration in 1961/62 was an average of 6380 per month compared to 8530 per month in 1960/61. (3) Of 108,291 settlers in 1960/61 87,383 were British or the nationalities of the Six or Seven (including Finland). In 1961/62 85,808 new settlers arrived of which 63,731 were of the afore-mentioned nationalities. (4)

Although the term "British" includes immigrants from other Commonwealth sources, the statistics show that the bulk of


the British migrants were of United Kingdom origin and that this source accounts for the reduction in numbers of British migrants. (5) The reduction in number of settlers from E.E.C. and E.F.T.A. countries thus slightly exceeded the reduction in total new settlers over this period.

(iv) Trade policies

Australia has been active in a number of international organisations over a period of years seeking a better deal for countries that export agricultural and other primary produce. At the Review Session of the G.A.T.T. the Minister for Commerce and Agriculture, the Rt. Hon. J. McEwen stated:

(6) "G.A.T.T. embodies a range of rules providing some stability and predictability in tariff relations which are important in trade in manufactured goods. It does not provide anything like a comparable degree of stability and predictability for trade in foodstuffs and raw materials."

Largely as a result of Australian efforts some improvements were effected in the G.A.T.T. at that session which helped to redress the balance of advantages given to different countries by that body. Australia, for instance, was given facilities, as a country dependent on the export of a few primary commodities and looking to the tariff as a means of diversifying its economy, to vary tariff bindings at any time. (7) Some safeguards were inserted against export subsidies on primary products capturing for the granting country more than an equitable share of world
trade (8), and as a consequence Australia was able to secure agreements with France and Germany limiting exports of flour to markets traditionally served by Australia. However, these provisions did not apply to surplus disposals under aid programmes and although both G.A.T.T. and F.A.O. provided for consultation by the exporting country in those cases there has undoubtedly been a tendency for such disposals to displace what might have otherwise been commercial sales opportunities.

These changes did little, however, in practice to rectify the advantageous position industrial countries enjoyed in regard to expansion of trade in relation to the primary exporting countries. Consequently largely on Australian initiative a committee was set up under Professor Haberler to make recommendations on these matters. However, the recommendations made by the Committee, that the industrial countries should moderate their agricultural protection so as to make room for increased imports and that aid programmes should take the form of cash, not commodities, were in practice not carried out. The F.A.O. also developed and obtained adoption of codes such as the principles to govern surplus disposals and price support which, although generally beneficial, have not altered the fundamental trade position.

In November 1961 ministers meeting under auspices of G.A.T.T. decided to request the setting up of commodity groups. Groups on cereals and meat have met but have not been able as yet to devise acceptable solutions to the problems presented. The main matter considered by the cereals groups has been the possibility of concluding world-wide commodity agreements on the lines discussed in the preceding chapter. It may be possible to make further progress in discussions when the question of British entry into the Community has been decided. Policy statements made by the Minister for Trade (9) indicate that Australia supports these initiatives. Australian support for an early United Nations conference on Trade and Development also indicates her concern that progress should be made as soon as possible to improve the outlook for commodity trade. Both the diminution of volume of this trade occasioned by protective policies in the industrial countries and the tendency for prices to become depressed are matters of concern. It may be noted in addition that the G.A.T.T. has not been effective in its bargaining processes in promoting the exchange of worth-while concessions on access for agricultural goods with industrial concessions; exchanges of concessions in the industrial sphere alone have, however, been successful.

If Australia loses its preferences in Britain there appears little doubt that Britain will not retain her preferences in Australia and in fact it appears that the Six would prefer Britain not to enjoy advantages which cannot

be accorded to themselves. Australia may still retain preferences for other Commonwealth countries but the G.A.T.T. prevents new or increased preferences so that worthwhile balanced agreements at more meaningful levels are not practicable. The G.A.T.T. "no-new-preference rule" is one of the few rules in G.A.T.T. that is strictly policed. (10) One way round this rule is to form a customs union or free trade area and the possibilities for Australia in this approach are considered in a subsequent chapter. It cannot be expected, however, that Australia would find it internationally politically practicable to enter into the type of partial union which has been tolerated between some under-developed countries (11).

Apart from its important 1932 agreements with Commonwealth countries, Australia has followed a policy of multilateralism in recent years. Agreements negotiated with countries such as Germany and Japan have spelled out reasonable access for Australian products in these markets but have not given these countries any assured quotas in the Australian market. (12).

It would be surprising, however, if some measure of bilateralism did not enter into Australian policy in order to find alternative markets for foodstuffs and metals.


(11) e.g. the free trade area between Nicaragua and El Salvador.

if Britain joins the E.E.C. and to widen the market for some secondary industries but just how this would be accomplished and whether or not it would accord with current international obligations cannot be predicted. It is sufficient to say that countries very often one way or another find ways of bringing their trade, when it is considerable, into better balance. One direction in which bilateralism is prevalent and has become almost respectable is in dealing with communist countries as many of these countries trade mainly on this basis. It appears, however, that these countries are prepared to import certain essential raw materials, such as wool without insisting that the other country takes equivalent goods in return.

Australian efforts, it has been noted, are now largely directed at improving access and price conditions for commodity trade. It has, however, also been noted that Australia is in regard to some commodities at a disadvantage in competing in certain markets with some other countries and that existing trade can largely be ascribed to preferential access. It will be necessary under the new conditions for Australia to be more competitive and in this respect she has a better chance in markets that are reasonably near, such as those of Asia, than in more distant markets. Whether or not under the new conditions and assuming that access is not seriously reduced, taking the world as a whole, it will be economically advantageous for Australia to continue to export some foodstuffs such as
butter and canned fruits, remains to be seen. The returns may, in fact, not make this worth while.

If, therefore, Australian exports of foodstuffs in particular do in fact decline, it will be advisable for Australian policy to be directed towards securing increased markets for certain types of secondary goods. If such market opportunities can be assured it may well be advisable for Australia to specialise in its secondary production to a greater extent than at present and to rely on imports of some types of goods now produced locally. Such a reorganisation of the industrial structure should be advantageous for the general Australian cost level and reductions in this level appear most necessary in the circumstances in which Australia is likely to find itself.
III. COAL, STEEL AND ATOMIC ENERGY

(a) The European Coal and Steel Community is of exceptional interest in the study of European integration as it is the outstanding example of a closely knit union which is in full operation. Moreover its experience in the field of monopoly control and in supranationalism is important for other international unions.

As has been noted in Chapter I, the origins of the Community were dominated by political aims and the acceptance of the Schuman Plan was widely held to be a decisive step to securing Franco-German amity for all time.

The political aims of the Community were not confined to the securing of peace, at least not simpliciter. One author has pointed out that the basic purpose of the Schuman Plan from the French point of view was the maintenance of the balance of power created by Germany's defeat in a form acceptable to Europe and to America. This was to be done by creating a new authority on supra-national lines, independent of all national governments. The plan formally involved the same sacrifice of national sovereignty by all the members of the Community and was therefore non-discriminatory in form; this made it acceptable to Germany and Italy who were jealous of their national status. (1)

(1) E. Strauss, Common Sense and the Common Market (1958) page 63.
The same author explains the need to limit Germany's power in this field by the predominance of the Ruhr steel industry due to ownership of exceptionally economic coal mines. (2) The advantage of cheap coal was denied to the French and other countries by the operation of the German coal cartel which fixed higher prices for export than for local sale. (3) The Treaty has not been entirely successful in shifting the balance of power away from Germany as the German steel industry, especially after the reversion to Germany of the Saar, soon once more outstripped that of France.

The central purpose of the Community is the formation and operation of a common market in coal and steel among the Six (France, the Federal Republic of Germany, Netherlands, Belgium, Luxembourg and Italy). It has been shown in Chapter I how the General Agreement on Tariffs and Trade has facilitated the formation of common markets that formerly were considered to be in breach of the most-favoured-nation clause of commercial treaties. One authority has pointed out that the Coal and Steel Community presented particular difficulties to the G.A.T.T. as it was neither a customs union nor a free trade area. Although barriers to trade were ultimately to be abolished within the

(2) E. Strauss, op.cit., page 65. (3) E. Strauss, op.cit. page 66.
Community, the external tariff was neither to be a common one nor was it to be left unchanged but the duties were to be harmonised, that it brought roughly into line. As this did not conform to G.A.T.T. concepts, a waiver of G.A.T.T. obligations had to be sought. (4) A further important point is that the Schuman Plan did not cover the whole economy, but only a sector of trade - a more important departure from the G.A.T.T. concept of a customs union than the uniformity of the tariffs of the members.

The same authority has pointed out that the situation was all the more delicate because of serious divergences in view among European countries about the Community. (5) Britain had stood aside because of its unwillingness to surrender sovereignty and as the negotiations progressed it became increasingly difficult for Britain to change its mind as the Community was being shaped to meet the particular interests of the Six. (6) More serious than Britain's coolness were the concerns expressed by the Scandinavian countries and by Austria. The former were anxious lest the Community might be a cover for the restoration of the old European steel cartel which might seriously prejudice Scandinavian consumers of steel by

establishing export prices considerably above prices ruling within the Community. Austria was also concerned about its small specialised steel industry, which depends on markets within the Community. (5) In the event G.A.T.T. granted a waiver, subject to annual reporting within the five-year transitional period, (1953 to 1958). In 1953, steel exporters in the Community, other than in Italy, formed a price cartel for exports to third countries. The purpose of the cartel was to keep the export price as high as the market would bear by preventing competition between Community exporters and consequently it is not surprising that during the transitional period the Scandinavians strongly attacked the actual operation of the Community as having the effect feared. (7) During the transitional period safeguards were afforded the high-cost Belgian coal industry and Italian heavy industry. (8) Completion of harmonisation of external duties by France and Italy was not achieved until February 1960.

The obligation to report annually to the G.A.T.T. during the transitional period has been important to the Community's external relations. The High Authority has

(7) Wm. Diebold, Junior, "The Schuman Plan", (1959), pages 492/4. (8) European Coal and Steel Community, Convention containing the transitional provisions, Sections 26, 27 and 30. The Belgian exception was never used (Wm. Diebold, Junior, op. cit. page 532.)
undoubtedly been able to exert more influence on steel export prices than if there had been no focussing of foreign complaints in the G.A.T.T. Groups in the Community interested in lower tariffs have had their hands strengthened. (9) External pressures on the Community, especially through the G.A.T.T., have prevented the Community being a more trade-diverting type of association. (10)

The Treaty does not in any way prejudice the regime of ownership of the enterprises subject to its provisions. (11) These may be nationalised or privately owned and their constitution may be changed as national governments desire. The Community rules are designed to secure a competitive market which works without price control and avoids the dangers of a producer's monopoly, indiscriminate dumping and price instability. (12).

The main institutions of the Community are the High Authority and the Council of Ministers. The latter was not in the original French draft and was apparently added by the Benelux countries. The High Authority is, generally speaking, the governing body. It is composed of nine members, eight of whom are chosen by agreement among the member governments and the ninth is elected by the

other eight. (13) Its members are to exercise their functions in complete independence. (14) This body is the expression of the supra-national character of the Community. It meets at least once a week.

The High Authority has the right to deal directly with the coal and steel enterprises of the Community without passing through national governments and these enterprises are responsible only to the Authority for their actions relating to the Treaty rules. The High Authority can direct the enterprises by "decisions" which are legally binding in every respect and by "recommendations" which are binding with respect to the aim they specify, leaving the method of compliance open. It may also influence enterprises by giving "opinions" which are not binding. (15)

The High Authority has some powers of an exceptional nature. It can levy fines on enterprises contravening the Treaty or not carrying out its decisions. (16) This power it has exercised on numerous occasions. The power of the High Authority to raise its own income by imposing a levy on enterprises has given it a high degree of independence. Moreover, it has important powers in relation to investment. (17) These powers are regarded with grave suspicion by the industrialists. (18) Its powers

in relation to investment have been exercised through surveys and compulsory submission of investment plans, opinions regarding which firms ignore at their peril. It has exerted some influence to reduce investment in steel plants requiring the use of scrap, of which the Community is fundamentally in short supply. (19) The powers of the High Authority in regard to cartels will be discussed separately.

The Community has experienced a change in methods of energy utilisation which has decreased the importance of coal as a source of energy from 60 percent of the total to under 50 percent. (20) This has created a "coal crisis" which commenced in 1958. Since the beginning of 1958 coal production has decreased by 7 per cent, one hundred collieries have been closed and 136,300 underground workers deprived of their livelihood. Readaptation has been relatively easy due to buoyant economic conditions. The Community has helped to finance redevelopment operations in Belgium in connection with the closing of coalfields. (21) Production of steel in the Community, which has increased from 42 to 73 million tons in nine years, is expected to expand less as a position has been reached where demand can be expected no longer to consistently outpace supply. The

High Authority intends to be more selective in its opinions concerning investment projects. (22).

The High Authority has powers of economic direction and control which make it more effective as a restrictive organ than the private cartels which it was intended to outlaw. In periods of shortage it can allocate supplies and fix maximum prices and in periods of acute depression it can impose minimum prices as well as output quotas. It has also the right to limit imports by requiring the imposition of restrictions. (23).

Writing in 1958 one author states "the plainfact is that the High Authority has failed as a supra-national organ capable of lifting control of the heavy industry of western Europe and above all of the Ruhr out of the hands of governments. The political centre of gravity has inevitably shifted from the High Authority to the Council of Ministers whose decisions are openly determined by the realities of power and not by the terms of a treaty." (24)

As has already been noted, the council of ministers was not desired by Schuman and was added as an afterthought.

Its concurrence is necessary for a number of important

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decisions of the High Authority. The increasing power of the Council was abundantly shown in 1958 when, owing to depression in the Belgian coal industry, the High Authority wished to declare a state of manifest crisis (25) and to regulate imports. (26) In this connection it needed the concurrence of the Council. This concurrence was not forthcoming due to the fact that the French and German producers wished to maintain a supply of cheap coal. It was therefore obliged to revise its plans and it obtained the Council's concurrence to limited subsidisation and readaptation assistance to the Belgian industry. (27)

This was clearly a blow at the supra-national principle and it is significant that France joined with Germany in-inflicting this defeat. General de Gaulle is known to dislike the supra-national principle on which his predecessors pinned so much faith. The President of the High Authority, Piero Malvestiti, referred to this matter before the European Parliamentary Assembly meeting at Strasbourg, on 1st April 1960. In referring to Belgium's appeal to the High Authority under Article 37 of the Treaty for action to protect its coal industry, he stated that the High Authority submitted its work in this connection to the judgment of

the Parliament and that it was conscious of having acted in full conformity with the spirit and letter of the Treaty. He also stated "the supra-national principle is proving not merely a political concept but also an instrument of economic policy. Once its validity has been established and confirmed, that instrument should be constantly worked up and reinforced." (28)

The provisions of the Treaty regarding agreements and combinations are detailed and more complete than in the Rome Treaty. Any transaction which would involve bringing about a concentration in the relevant industry must be authorised by the High Authority. (29) The first reaction of the High Authority to its assumption of power in this field was to proceed cautiously. (30) It has since been accused of timidity in its attitude to cartels. (31) One author states that it has "failed utterly in its half-hearted attempts to carry out its duties." (32) The High Authority has, nevertheless, not been inactive in this field and has used its powers of imposing fines in addition to promulgating a number of decisions. It has had a long battle with the Ruhr Coal Syndicate and the latter has had to adapt its

ways, though it remains fairly unscathed. (33) (34) It appears to be having some success in modifying the Oberrheinische Kohlenunion (35), and has eventually succeeded in arranging for supervision of the French coal import monopoly, whilst reserving its position on the effectiveness of the new French regulations until it is seen how these work out. (36) One author has explained that in its early days the High Authority did indeed seek to increase competition in the coal industry. But governments were not willing to tolerate the waste due to instability created by competition. The High Authority therefore thence had the task of trying to assure the fruits of competition without in fact creating a competitive situation. (37).

Many provisions in the Treaty are similar to those in the later Rome Treaties. These include the provisions for a Parliament and Court of Justice; Transport; Adaptation of workers to new employment; Wages and Movement of Labour.

The High Authority has not been able to do anything directly about wages. Not only have diverse systems of social services made wage comparisons very difficult but also different degrees of productivity in the various countries

make equalisation of wages economically undesirable. Another field in which the efforts of the High Authority have met with mixed success is in adaptation. A scheme for moving workers from southern French coalfields to Lorraine was unsuccessful mainly because the workers did not wish to move. A scheme to tide Italian steelworkers over whilst the industry was being modernised has been described as a belated supplement to a social security grant rather than a means of providing adaptation. (38) One author, writing in 1959, considered that the provisions of the Treaty regarding free movement of labour had led to no more an agreement to permit movement of certain skilled categories of workers, many of whom were unlikely to want to move. This author noted that the large movement of Italian unskilled labour was still regulated by bilateral agreements outside the Treaty and that such movement was unlikely to be freed from restriction. (39)

An agreement of association was signed between the E.C.S.C. and Britain in 1954. This agreement has led to the adjustment of steel tariffs closer to a common level and has enabled both sides to gain a fuller knowledge of

the state of the coal and steel markets in the other area. (40) Britain applied to join the Community in 1961. If Britain accedes to the Treaty, the coal production of the Community would be practically doubled, rising to over 400 million metric tons, exceeding the present production of the United States and considerably larger than that of the U.S.S.R. (40) The fact that the steel industry in Britain is nationalised presents some difficulties in relation to the Treaty provisions regarding competition.

Some economic aspects of the E.C.S.C. have been discussed by Tibor Scitovsky. (41) He points out that the effects of sector integration on welfare may be either favourable or unfavourable. For example, if the Community leads to a reduction of Belgian coal production and an increase of German coal production, resources will be shifted into other industries in Belgium and out of other industries in Germany. Whether this leads to an increase in welfare or not depends on whether these resources can be used more efficiently in Belgium and used less efficiently in Germany. He points out that in Germany the additional resources needed in coal mining could probably be withdrawn from import-competing industries if the improvement in the balance

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of payments leads to a more liberal import policy; they would be likely to be diverted mainly from export industries if Belgium aimed at the same time at increased self-sufficiency, especially if this led in turn to a general restriction of trade also in third countries. The question whether the effects of integration would be beneficial or otherwise therefore depends largely on whether the economic atmosphere does or does not favour the expansion of trade. He concludes that the liberalisation of trade in fields other than coal and steel is almost certainly a necessary condition for rendering the reallocation of output beneficial rather than harmful.

Moreover, in the case cited, if factors move from Belgium to Germany, there is likely to be a worsening of the Belgian balance of payments position corresponding to the shifts in production, less the consumption of importables and exportables of the transferred resources. In addition there will be a once-for-all transfer of monetary resources with the factors, the effects of which may last over a period.

As an offset to the very doubtful benefit from reallocation of resources, Scitovsky does, however, see some real benefit in the cheapening of products in the sector. This benefit is particularly evident in relation to steel as cheap steel would favour the propensity to invest, which is generally regarded as desirable. In regard
to coal the same effect would take place but there might also be a harmful effect, the encouragement of coal utilisation in preference to more efficient sources of energy.

As an overall assessment of the effect of the E.C.S.C. it may be stated that there is no indication that it has retarded growth in the Six and that, as it has facilitated the rationalisation of the industries concerned it has prima facie been beneficial. Faced currently with a prospect of downward adjustment in the coal sector the Community may well exert a retarding influence in switches to other sources of energy; in this connection difficulties appear to have arisen in regard to freeing trade with certain oil-producing territories and in regard to the use of natural gas from the Sahara and there may be further conflicts between the use of nuclear and traditional energy sources. The existence of an integrated industry does, however, facilitate any adjustments that may be necessary and it has undoubtedly also made much simpler the formation of the E.E.C.

Trade between Australia and the Six is small and the formation of E.C.S.C. would therefore have had little direct effect on Australia. The Community is competitive with Australia in steel products in certain markets such as
India and it may be that the integration of the European industry has diminished Australia's chances in such markets but this is difficult to determine. Loss of certain preferences in Britain by reason of the association agreement has adversely affected a useful outlet for certain lines of Australian production when, from time to time, excess supply positions develop. Australia has been dependent on Britain for some import lines of steel but this dependence is diminishing. Competition from the United States is probably adequate to offset any monopoly effects on supply prices of European integration in this sector.

Skilled migrant workers in the steel industry have been useful to the development of the Australian industry. Integration in Europe may have reduced the number of such workers willing to migrate but rationalisation of the European industry may have had a somewhat contrary effect by releasing surplus workers.

(b) **The European Atomic Energy Community**

The European Atomic Energy Community (Euratom) is based on a customs union between the Six in matters relating to nuclear energy and may be regarded as an acceleration in that sector of the customs union provided for in the European Economic Community Treaty concluded simultaneously in Rome.
Within a year of entry into force of the Treaty, duties and quantitative restrictions were, as provided for in the Treaty, abolished on trade between member states on products in lists A1 and A2 annexed to the Treaty. (42) The lists include ores and compounds of uranium, plutonium, thorium, deuterium, nuclear reactors, isotopes, packing materials and vehicles for transport of radio-active materials. Similar abolition of trade barriers is provided for products in list B, which includes parts for nuclear reactors, lithium ores, metals of nuclear quality and numerous specified articles of equipment and apparatus, provided that a common external tariff has been applied and that the Commission of Euratom certifies that they are intended for nuclear purposes.

The Treaty is not confined in effect to acceleration of the common market in nuclear materials. It also provides for the constitution of an agency whose purpose is to secure equality of access of materials for all users and that has an option to acquire all nuclear supplies within the Community. (43) Such materials must be offered to the agency and the rights of owners to dispose of materials not required by the agency are restricted. An owner may,

(42) Treaty establishing the European Atomic Energy Community, Article 93; the Treaty entered into force on 1 January, 1958. (43) Article 52.
for instance, only export with the sanction of the Commission and provided also that he offers the materials for export on terms no more favourable than those of his prior offer to the agency. (44) Moreover, certain types of materials, termed "special fissile materials", (45) are ipso facto the property of the Community and states and firms can only deal with them in defined ways. (46) Only the agency can export such materials. (47) The agency has an exclusive right to purchase materials from outside the Community and is to be advised of requirements for such materials. Users may only purchase materials directly from abroad in exceptional circumstances. (48) The agency is entitled to build up stocks. (49) Besides its rights it has an obligation to fulfil orders. (50) It is subject to the control of the Commission in some respects. The Commission must approve agreements regarding delivery of products within the control of the agency. Small transactions may be exempted as are contracts for processing and return to the supplier. (51)

The Council of Euratom may in some circumstances fix prices for nuclear materials. (52)

Although Euratom may be compared with the British and American atomic energy authorities, it is different from these in that it has no functions relating to the use of atomic energy for military purposes. (53) The object of the Community is "to contribute to the raising of the standard of living in member states and to the development of commercial exchanges with other countries by the creation of conditions necessary for the speedy establishment and growth of nuclear industries." (54) The main lines of action by which the Community is to achieve these aims is by developing research and ensuring the dissemination of technical knowledge, by the application of uniform safety standards, free movement of labour and capital, ensuring construction of basic facilities, particularly by encouraging business enterprises, ensure regularity of supplies and safeguard diversion of materials from purposes for which they are intended. (55).

The Community is empowered to make agreements with other countries. (56) In November, 1958 Euratom concluded an agreement with the United States which assured it considerable

financial and technical help from that country. In February, 1959 Euratom made an agreement with Britain. Besides provisions of a general nature regarding exchange of information, patent licences, technical advice and training and assistance to firms purchasing reactors, this agreement provided for the supply of nuclear fuel from Britain to Euratom. A standing committee on co-operation is also set up. Two agreements were signed with Canada in October 1959. The first, with the Canadian Government, provided for exchange of data, equipment and materials whilst the second, with the Canadian Atomic Energy Corporation, provided for a joint research development programme. (57)

It will have been gathered that the Treaty provides for a Council of ministers and a Commission. It also provides for an Assembly, a Court of Justice and an Economic and Social Committee.

Atomic energy is a field which is universally regulated by national agencies. The creation of a joint national agency between the Six and its separation from matters of defence should be beneficial to economic development.

Australia exports uranium ores and monazite and imports radio-active isotopes. This trade is not covered in

(57) Keesing's Contemporary Archives, 16574, 16654, 17141.
the official trade statistics but contracts for supply of uranium ores to the United States have been discussed in Parliament. There are markets and sources of supply in Britain, the Community, Canada and the United States. It is not apparent that integration in Europe will have much effect on Australian trade. Australia has not concluded any agreement with the Community, so far as appears on the record. This may be due to the lack of development to date of industrial use of atomic energy in Australia.
IV. THE ORGANISATION FOR EUROPEAN ECONOMIC COOPERATION AND THE ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

The development of the O.E.E.C. and the nature and development of its trade liberalisation programme have been outlined in Chapter 1.

The original liberalisation of up to fifty per cent was accomplished without much difficulty on the part of most countries but when liberalisation was carried beyond that stage there appears to have been at least a commencement of greater competition in the area. There had been some discrimination for currency reasons as between countries in the area but the Code of Liberalisation adopted in August, 1950 provided that as soon as the European Payments Union came into effect such discrimination would cease. One writer notes "in addition to their immediate importance, the rules for trade equality, coupled with the E.P.U., gave some meaning to the concept of western Europe as a 'trading area'. Discrimination within the group was rejected, at least in principle. By virtue of this decision, and those removing quotas, countries in the O.E.E.C. assumed certain obligations to other members (and for certain rights against them) that were different from their rights and obligations in dealing with countries outside the organisation. Previously each
country could treat other members of the O.E.E.C. differently; now in important commercial matters, it is obliged to treat them equally." (1)

Not only was liberalisation to be equally applied by members to all other members but also after 1 February, 1951 quotas were to be equally available to all members. It was left to O.E.E.C. to decide what was meant by equality in the administration of quotas and some exceptions to the rule were provided.

Generally speaking the liberalisation programme was faithfully carried out. As a result of the Korean war difficulties appeared in certain countries. First Germany had a payments crisis which was solved with the aid of action in O.E.E.C. since when her payments position has been exceptionally strong. Both Britain and France then entered periods of difficulty. However, by the end of 1957 the major European currencies were declared externally convertible, since when there has been a progressive emergence of these countries from balance of payments difficulties and formal convertibility was attained early in 1961. Import restrictions that remain in the major Western European countries both for trade within and without the area are protective in nature and not related to balance of payments difficulties.

(1) Wm. Diebold, Junr., Trade and Payments in Western Europe, (1952), page 175.
Although there has been considerable movement since 1957 in removing restrictions on imports from outside the area, some discrimination still remains against such imports and in favour of imports from within the area. In the removal of this discrimination there has been a tendency to favour the United States and Canada before other countries. This is notably so in the case of France and Austria and it is also a facet of the liberalisation programme of E.E.C. under the common commercial policy.

Despite the requirement that at least seventy-five per cent of import trade should be liberalised in each category of goods - food, raw materials and manufactures - there was a considerable lag of liberalisation in the agricultural field. This was possible for two reasons. Many agricultural products could only be imported by state monopolies and it was apparently considered too difficult to determine whether or not such goods were liberalised, so they were excluded from the programme altogether. Secondly, as the liberalisation percentages were based on trade in a base period, products, trade in which was prohibited or severely restricted at the base date have either no or a negligible weight when the overall liberalisation percentage is calculated if the restrictive treatment is continued. It was therefore technically possible to keep within the liberalisation requirement by freeing only products which
had been traditionally traded in quantity. Moreover, products could be chosen for liberalisation which were protected by high tariffs. The limit of ingenuity in this respect was probably reached in Sweden where variable import levies, depending on seasonal differences between local and import prices, were supplemented by import restrictions, which, being emergency measures, fell outside the O.E.E.C. rules. This system appears to have influenced the European Economic Community.

Triffin has made some interesting comments on the economic aspects of the O.E.E.C. liberalisation programme. (2) First he pointed to the fact that the European Payments Union area covered a very large proportion of world trade and that in 1949 imports from non-members were practically limited to essentials not obtainable within the area. There was therefore much scope for trade creation and little for trade diversion. Although he ignores the fact that O.E.E.C. liberalisation did not in all cases extend to the full E.P.U. area (e.g. the outer sterling area), Triffin's point is a good one.

Secondly Triffin argues that the liberalisation percentages became sufficiently great so as to ensure that some

(2) R. Triffin, The Size of the Nation and its vulnerability to economic nationalism, pages 254/7 of "Economic Consequences of the Size of Nations" (International Economic Association) (1960)
of the benefits obtained in a customs union (i.e. of competition) were obtained. Subject to the limitations of the method of computing percentages of liberalisation discussed above and that tariffs still remained on many items which it was desired to protect, this also has some significance.

In addition Triffin points out that liberalisation between countries in balance of payments difficulties but enjoying full employment will be ineffective as members can only expand exports to each other at the expense of exports to third countries or by aggravating inflationary pressures. If, however, the members have unemployment, liberalisation will tend to increase mutual trade and improve the employment position. He concludes that any resulting discrimination against imports from third countries will tend to be self-correcting. By this he is evidently referring to the fact that any increase of trade between the members that displaces imports from outside countries will be accompanied by an increase in general economic activity tending to increase imports generally. Certainly the formation of the O.E.E.C. appears to have increased competition within the area and been accompanied by a general rise in economic activity. The capacity of some members, such as France, to import from outside the area, did, however, remain limited. This may be because liberalisation tended to increase French imports of, say German industrial goods, but the types of goods exported
by France, many of which were agricultural products, did not benefit to the same extent by liberalisation.

The O.E.E.C. liberalisation programme has stood in an ambiguous position in relation to the G.A.T.T. Whilst they were in balance-of-payments difficulties, the main members advised the G.A.T.T. that they were discriminating in accordance with Article XIV 1 (b) of the G.A.T.T. This provision which refers to the rules of the International Monetary Fund is somewhat difficult to interpret though it has been accepted that there should be a "currency" reason for discrimination. Some G.A.T.T. members have not accepted that there was a valid currency reason for O.E.E.C. liberalisation which was not extended to countries such as the outer sterling area, forming part of the E.P.U. The United States, which was the architect of O.E.E.C., has, however, been a staunch defender of O.E.E.C. liberalisation, whilst pressing for the removal of dollar discrimination. In recent years liberalisation in favour of North American countries by the western European countries has gone further than for other G.A.T.T. members. Since the advent of external convertibility in late 1957 and the subsequent emergence of the major western European countries from balance of payments difficulties, the
opposition to discriminatory liberalisation has become more vocal. (3).

Liberalisation as a programme has not survived the winding up of the O.E.E.C. and its replacement by the Organisation for Economic Cooperation and Development, though existing liberalisation appears to have been preserved by the individual countries.

The effect of O.E.E.C. liberalisation on Australia

The ninth annual report of O.E.E.C. (4) stated that it was not possible to carry out liberalisation policies before a substantial degree of economic stabilisation had been achieved but that there was nevertheless a reverse side of the picture as recovery and financial stability were enormously facilitated by the freeing of trade. The impressive development of post-war European production could not, the report states, be separated from the even greater development of intra-European trade.

Consequently there is a strong presumption that the O.E.E.C. liberalisation programme has been beneficial to Australia by increasing the prosperity of its European markets. Not only would this effect have increased Australian exports

(3) The Ninth Annual Report of O.E.E.C. (April, 1958) stated that at that time Britain, the Benelux countries, Denmark, Greece, Italy, Norway, Sweden and Switzerland extended their liberalisation measures to the outer sterling area and Germany applied to that area a special liberalisation list of practically the same scope as that applying to O.E.E.C. members. (page 74)

(4) page 54.
to continental Europe, which are largely of wool and skins, but would also have strengthened the British market which has been the backbone of demand for the majority of Australian export commodities.

It is likely therefore that the trade created for Australia would have exceeded any lost through diversion. In the British market all liberalisation effected under O.E.E.C. appears to have been available to imports from Australia and in recent years the same can be said for Greece, Italy, Benelux, Switzerland and the Scandinavian countries. The magnitude of trade diversion causing loss to Australia has probably not been great in Germany. Trade in apples and pears, for instance, were liberalised but seasonal factors would have reduced the impact of unrestricted entry of Italian fruit. Wool and skins were not produced for exchange amongst European countries nor except in less developed countries, such as Turkey, were there any restrictions at all in this sector. The effect of apparently severe discrimination by France and Austria under the O.E.E.C. programme may not have greatly affected Australia because of the nature of the products liberalised but this discrimination has now become an anachronism. In this connection both France and Austria have followed a policy of high protection and self-sufficiency on the agricultural side. With the aid of
substantial tariff preferences room has been found for imports from the French colonies and former colonies; any preference in import licensing, however, does not appear related to the O.E.E.C. programme. Some of the trade from these territories is of tropical products but much is of produce that could be supplied by Australia.

In considering the lack of trade in some commodities such as meat and dried vine fruits that could have been supplied by Australia to continental Europe, it appears that the greater attractiveness of the British market with its tariff preferences and meat agreement guarantees has caused continental markets to be treated as of secondary importance. On some commodities such as canned fruits, Australian products may not have been competitive with other suppliers. In the case of grains, however, Australian opportunities have been affected by domestic production and external policies.

O.E.E.C. liberalisation has cast a shadow on certain of the overseas territories of the member states. Australian exports to New Caledonia appear to have been adversely affected by discrimination in favour of O.E.E.C. countries and more recently by measures taken under the Rome Treaty.

The more serious trade discrimination in O.E.E.C.
countries so far as Australia is concerned appears to have derived from bilateral agreements which were unconnected with the O.E.E.C. programme. Examples of such agreements were those under which Germany imported grains from Sweden and France; the latter agreement has been continued in the context of the Rome Treaty but is now replaced by the common agricultural policy. There are also grains agreements between France, Morocco and Tunisia. Some other products of interest to Australia have also been the subject of similar agreements.

It may therefore be concluded that the beneficial effects of O.E.E.C. liberalisation on Australia have almost certainly outweighed the adverse effects but that the time has come when any remaining discrimination should be removed. The O.E.C.D.

As has been noted in Chapter 1, the O.E.E.C. has now been replaced by O.E.C.D., which includes Canada and the United States as full members. The activities of the O.E.C.D. have been to continue the general co-ordination activities of the O.E.E.C. which were also described in some detail in Chapter 1 and to continue to work on such matters as the liberalisation of invisible transactions but not on trade liberalisation, which it was felt was inappropriate to current conditions of currency convertibility.

The O.E.C.D. has also a development assistance
programme which is spreading the burden of assistance to less developed countries more evenly amongst the industrial countries. The development of these countries will be beneficial to Australia in a number of ways, including trade. The increasing concern of the European countries for the welfare of less developed countries coincides, however, with an unconcern for the trade interests of the more wealthy developing countries such as Australia. The effects of this unconcern have been evident in relation to the negotiations for Britain to join the E.E.C.

It must not be thought, however, that the O.E.C.D. will necessarily continue its present unimportant role in the trade field. It has indeed, already, given some attention to problems of trade in butter and milk powder. The O.E.C.D. was also chosen by Mr. Orville Freeman, United States Secretary of Agriculture, to make an important policy declaration in November, 1962 regarding agricultural trade. If Japan, which joined the Development Assistance Group in 1960, should become a full member of O.E.C.D., this might tend to promote increased activity of this body in the field of trade.
V. AUSTRALIAN PARTICIPATION IN SCHEMES OF INTEGRATION

There has been a reaction in other parts of the world to economic integration in Europe that has taken the form of consideration of the advantages of regional integration elsewhere. In some cases this has led to actual schemes which have been implemented; this is the case in Latin America. In other cases smaller schemes have been developed and appear likely soon to be implemented; this is the case in Africa. In Asia, however, insufficient advantage has been seen in economic integration to date though one small loose organisation between four south-east Asian states has been brought into being; this body to date has not, however, attempted to set up a customs union or any analogous preferential association.

The possibilities for Australian participation in schemes for economic integration will be considered under three heads - integration with Commonwealth countries such as New Zealand, Canada and Rhodesia and Nyasaland - association with the European Economic Community - association with Asian countries.

(a) Commonwealth countries

The following proportions of Australian external trade were effected with the three Commonwealth countries mentioned above in 1960/61:
Australia 1960/61

Proportion of trade with selected Commonwealth countries

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Zealand</td>
<td>6.6%</td>
<td>1.5%</td>
</tr>
<tr>
<td>Rhodesia and Nyasaland</td>
<td>0.3%</td>
<td>0.4%</td>
</tr>
<tr>
<td>Canada</td>
<td>1.9%</td>
<td>4.2%</td>
</tr>
</tbody>
</table>

SOURCE: Overseas Trade Bulletin (calculated).

The proportions of the trade of these countries effected with Australia in 1960 were as follows:

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Zealand</td>
<td>4.4%</td>
<td>18.0%</td>
</tr>
<tr>
<td>Rhodesia &amp; Nyasaland</td>
<td>1.4%</td>
<td>1.9%</td>
</tr>
<tr>
<td>Canada</td>
<td>1.9%</td>
<td>0.6%</td>
</tr>
</tbody>
</table>

SOURCE: United Nations yearbook of International Trade Statistics. (calculated)

New Zealand

Economic integration with New Zealand appears the most practicable in this group both because of the relatively large proportion of trade involved and because of geographical propinquity. It is evident, however, that New Zealand would expect to increase its exports to Australia in such circumstances more than its imports from Australia, in order to bring trade into better balance.

The composition of Australia's import trade from New Zealand (1) over the period 1 July, 1958 to 30 June, 1961 was -

(1) Calculated from Overseas Trade Bulletins
Pulp and paper 52 per cent; Timber 11 per cent; Wool 9 per cent; Seeds 6 per cent; Fish 4 per cent; Horses 3 per cent; Vegetables 2 per cent and other items 13 per cent. Australian export trade (1) to New Zealand was made up of Iron and steel 20½ per cent; Oils 15½ per cent; Wheat 9 per cent; Vehicles 11½ per cent; other metals, manufactures and machinery 10 per cent; Chemicals and plastics 5½ per cent; Sugar 5 per cent; Fruits 3½ per cent; Timber 2½ per cent and other items 17 per cent.

Australian export trade to New Zealand besides being much larger in size than New Zealand's export trade to Australia, is more varied in content as it contains a variety of manufactured items. One substantial export, mineral oils, is derived from imported raw materials.

The chief immediate benefit to New Zealand from integration would be an expansion of pulp and paper exports to Australia. The capacity for such expansion already exists in New Zealand and much of Australian requirements is imported from Canada and Europe. Although expansion of this trade would be trade-diverting it is to be noted that New Zealand costs are not out of line with those in other parts of the world and that any loss of welfare through this diversion would be small. At present it cannot be foreseen that there would be much opportunity for New Zealand to market meat and dairy produce in Australia as Australia is a large exporter of these products. The Australian dairy industry is subsidised but much of the industry could exist
without the subsidy and there is room for increase of efficiency in organisation. (2) However, it is likely that any joint scheme of overseas marketing would provide for a reduction of the Australian exportable surplus of dairy products. Meat is, however, of such exceptional importance in the development of the north of Australia that it is not possible to conceive any scheme of deliberate reduction of production.

It is apparent that the opportunities afforded New Zealand's traditional exports through integration are limited in area and it would therefore also be anticipated that there would be planned development of industry in New Zealand to serve the combined market. (3)

There is a great deal of apparent benefit for Australian industry through integration with New Zealand; that country is already the major export market for Australian manufactures and the opportunity to replace goods imported from Europe and America would be much increased under integration. The chief difficulty would appear to ensure that the benefits are not too one-sided and that New Zealand industry is not denied the chance to further develop. In this connection care will have to be taken that Australian industry does not engage in any form of dumping in New Zealand.

(2) The Report of the Dairy Industry Committee of Enquiry (1960) brings out these points. (3) In the semi-manufactures field the proposal to smelt Australian bauxite at Invercargill, some of which would be re-exported to Australia as aluminium, is illustrative
Despite the mutual advantages likely to result from integration the area would still be largely dependent on overseas sources for many raw materials and for much machinery and access would need to be afforded to the produce of Japan and other countries with whom a sizeable export trade was conducted.

Integration would not need to involve great changes in the cost structures of industry in the two countries. This would make it easier to achieve but highlights the incompleteness of the solution as there would be a tendency for Australia/New Zealand to remain a relatively high-cost area vulnerable to all influences affecting the prices of its primary exports. Whereas, therefore, integration with New Zealand is seen as a useful step it will not obviate the need for other adjustments to ensure that the area becomes economically strong.

Rhodesia and Nyasaland

Australian trade relations with the Federation are governed by a bilateral preferential arrangement but trade remains rather small. Imports from the Federation in the three years ended 30 June, 1961 consisted of Tobacco 86 per cent; Metals 9 per cent; Asbestos and Chrome ore 2 per cent and other items 3 per cent. Exports to the Federation consisted of Wheat, Flour and Malt 73 per cent; meats and milk 13 per cent; Tallow and other fats 5 per cent; Agricultural machinery 3 per cent and other items 6 per cent. (1)
On the import side free entry for Rhodesian tobacco would considerably reduce the size of the highly protected Australian tobacco industry. The copper industry might also suffer unless special sanction was provided for subsidisation of mines. The opportunity for expansion of trade in other traditional products of the Federation appears to be small. On the export side opportunities for expansion of Australian trade in agricultural products would be limited to maintain Rhodesian domestic production. In the industrial sphere the Federation has shown, by breaking off its proposed customs union with South Africa, that it wishes to retain full freedom to develop its industries. A further obstacle to integration with Australia is the fact that the Federation may associate with the E.E.C.

There are therefore considerable obstacles to integration between the Federation and Australia to which may be added differences in the labour structure and geographical distance. It does not appear that integration would be practicable.

Canada

Australian exports to Canada in the three years ended 30 June, 1961 were composed of Sugar 42 per cent; Meats and sausage casings 20 per cent; Fruit, dried and other preserved 20 per cent; Wool 11 per cent and other items 7 per cent. Australian imports from Canada over this period were Aluminium 14 per cent; Vehicles 13½ per cent; other metals, manufactures and machinery 17 per cent; Timber 12½ per cent; Chemicals, plastics and rubber substitutes 7 per cent; Asbestos 5 per cent and other items 8 per cent. (1)
Trade is rather small in both directions but is generally twice as important from Canada to Australia than in the reverse direction. Australian exports to Canada have been fostered by tariff preferences and in the case of sugar by the Commonwealth Sugar Agreement. The opportunities to expand such exports in the meat and dairy products field are limited by the desire of Canada to protect its own production. The outlook for expansion of Canadian exports of aluminium, pulp and paper to Australia is poor because of expanding production in Australia and New Zealand. For quarantine and other reasons Australia is unlikely to want Canadian wheat. There is, however, room for expansion of Canadian exports of manufactures to Australia.

As in the case of New Zealand there are difficulties in the primary production field in any scheme of integration. In other fields the advantages to Canada seem to outweigh those for Australia and it is not so easy to envisage the same degree of cooperation to balance off these advantages as could take place with New Zealand, if only because of the contiguity and close trading relations between Canada and the United States and the influence this has on the structure of Canadian industry.

(b) Association with European Economic Community

The proportion of Australia's trade with relevant European countries in 1960/61 was as follows: -
Australia. Proportions of trade in 1960/61 with 18 European countries

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>21.8</td>
<td>35.8</td>
</tr>
<tr>
<td>The Six</td>
<td>16.8</td>
<td>11.6</td>
</tr>
<tr>
<td>Rest of E.F.T.A.</td>
<td>1.0</td>
<td>4.5</td>
</tr>
<tr>
<td>(including Finland)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ireland, Greece, Spain, Turkey</td>
<td>1.1</td>
<td>0.3</td>
</tr>
<tr>
<td></td>
<td>40.7</td>
<td>52.2</td>
</tr>
</tbody>
</table>

Source: Overseas Trade Bulletin (calculated)

Although the percentage of Australian exports taken by western Europe has been declining, the area is still a very important market for Australia. On the other hand Australia, although one of Britain's largest individual markets, is a less important trading partner so far as western Europe is concerned.

Trade with Australia. 17 European countries. Percentage of total trade. Year 1961

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th>Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>5.3</td>
<td>4.1</td>
</tr>
<tr>
<td>Six</td>
<td>0.7</td>
<td>1.3</td>
</tr>
<tr>
<td>Rest of E.F.T.A.</td>
<td>0.9</td>
<td>0.3</td>
</tr>
<tr>
<td>(excluding Finland)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ireland, Greece, Spain, Turkey</td>
<td>0.2</td>
<td>0.9</td>
</tr>
<tr>
<td>Total of above</td>
<td>1.6</td>
<td>1.7</td>
</tr>
</tbody>
</table>

Source: O.E.E.C. Trade Statistics (calculated)
In view of the fact that Australia is of little importance as a market to the Six and that the bulk of Australia's trade with the Six is in commodities, trade in which is unlikely to be affected by mutual integration, it is only useful to consider the possibility of integration with a Community including Britain.

It has already been concluded that even a Community including Britain would not aim to be a large importer of foodstuffs. Nevertheless the possibility of policies being followed allowing a substantial import of foodstuffs is greater in the case of a Community including Britain than in the case of one excluding Britain. Moreover the economic stature of a Community including Britain would be greater and this would facilitate the assumption of responsibility for disposing of agricultural surpluses by donation to less-developed countries in a joint effort. Some advantage could therefore be obtained by Australia on the agricultural export side by association with a Community including Britain.

From the point of view of the Community the association of Australia extends the Community into a new geographical area, thus tending to make it more unwieldy than at present. The advantage for the Community would lie in the Australian market for manufactured goods.

If full association were sought on the lines of Greek association and it is not possible currently to envisage the Six considering anything less than this, it would be necessary for Australia after a transitional period to grant free entry. But the inclusion of countries such as Ireland and Denmark would render the problem as difficult as before. New Caledonia is associated, but this is only a small territory.
to Community goods. Some exceptions could be made for developing industries but such exceptions could hardly outlast the transitional period and would thus probably take the form of exceptions to the rhythm of tariff reduction and an extension of the transitional period in which these special cases are removed.

This is a scheme which in this century has never been contemplated in Australia even in regard to the products of British industry. It has always been contemplated that the cost level in Australia would exceed that in Europe and that practically everything manufactured in Australia would require a measure of protection; though industries whose costs were too far out of line and were considered not "economic and efficient" would be allowed to go to the wall.

The Australian tariff is part of the political environment and acceptance of its eradication in regard to European products would be revolutionary. The Prime Minister's words in 1929 "the Australian policy of protection is based upon the belief that such a policy tends to accelerate our development and to increase our national prosperity" (6) still holds good. The statement was not a random one as the Prime Minister had at time the benefit of the opinions of a distinguished group of economists to the same effect. (7) Today the opinion is still expressed that the tariff promotes "population growth" and a "greater stability of national income and employment". (8) Importance is also attached to the selective operation of the tariff in accordance with the principles guiding the Tariff Board. (9)

is the instability of export markets (10) but this is also given as a reason for economic integration. (11) A further point is that a stable and assured domestic market is regarded as a prerequisite for the securing of economies of scale by Australian industry. (12)

The first point to note is that the reasons for high costs in Australian industry should be susceptible of analysis. If indeed there are elements in the situation that cannot be rectified in a foreseeable period there would be a strong case for asking the Community for special terms of association allowing the retention of a measure of protection for Australian industry. There is one aspect that is, however, reasonably clear and that is that Australian industry could not under such an association enjoy the measure of security that it does at present. It would need quickly to adapt itself to new techniques and methods of management as they developed elsewhere in the Community.

Secondly it should be noted that Greece has already entered into an association with the Community providing for the formation of a customs union over an extended transitional period. Portugal, Norway and other countries have entered into an association with Britain for a free trade area and are contemplating a customs union with the Community. These countries are relatively under-developed industrially. Enquiry must be made as to the reasons these countries are so confident that the result will be beneficial to them. One

obviously beneficial result is assurance of a market for primary products which is also an attractive feature for Australia. However, these countries are anxious to increase their industrialisation and assistance will be given them to do so. Australia would also look to the Community for capital. Moreover, there is no doubt that in either case firms in the industrial countries will form subsidiaries in the less developed countries where the benefit of their techniques can be obtained.

Industries that were developed in the peripheral countries would be able to export to the whole Community. Although their geographical situation might appear to render them less advantageously placed to supply the Community than more centrally situated plants, nevertheless in some cases the countries concerned are favourably situated to export to areas such as the near East and Africa. Initially labour costs in these countries would be less than in the industrialised though this might not be a permanent feature.

If Australia were associated with the Community it would also have the Community as a market but the geographical factor would be more serious than in the case of the peripheral countries. However, freight costs would also operate as a measure of protection to domestic industry. Australia would also be favourably situated to export to Asia and Africa and the west coast of America. Labour costs in Australia are not low and the maintenance of a high standard of living is essential to attract immigrants. However, the experience of North America indicates that the costs of high
real wages can be offset by increased productivity.

It has previously been noted that many economists consider the importance of economies of scale has been greatly exaggerated. Although it appears to be accepted that there are significant economies to be obtained in integration of countries of population ten to fifteen millions (13), it is also accepted that integration of countries of this size will involve readjustment rather than dangers. That the Australian market, together with limited export markets, is large enough to support economic industries is indicated by the experience in iron and steel and motor vehicles. The economies to be secured by expanding the market and the scale of production are, however, of considerable importance and have even been advanced as reasons for Britain with its existing large markets, joining the Community (14). There is no doubt therefore that association with the Community would involve more specialisation in Australian industrial development. That specialisation is a practicable proposition is indicated by the experience of countries such as Sweden and Switzerland which have been very successful in selling specialised products over tariff barriers.

Whether or not Australia associated with the Community, some industrial readjustment will be necessary. The primary produce sector will no longer be able to afford to bear the burden of protection of industry. (15)

Other advantages accruing from association would be the ensuring of capital for development and the facilitation of the continuation of European migration. Disadvantages might arise through a tendency to cut down import trade from Asia; these would have to be corrected as a close association with Asia both in the field of trade and otherwise appears essential. Another matter that would need careful examination is how continued development especially of outlying areas could be assured in the new circumstances; such development involves risks and appears to require rewards associated with mildly inflationary policies which may not be compatible with association. These are problems that present themselves in some form or another irrespective of association. Another essential matter is that imports from the Community must in no wise be dumped or sold at marginal costs in Australia in competition with Australian industry; this is a problem which is not neglected in the Rome Treaty.

Association with the Community might be incompatible with retention of preferences in the Canadian market and this may lose Australia some trade in sugar, canned fruit and other commodities. The volume of such trade is, however, not very large and the preferences in question may not necessarily endure in face of the break-up of the preferential relationship with Britain. Some trade problems might also arise with the United States but this country has a very favourable trade balance with Australia and is committed to non-discrimination.
Before association with the Community can be considered as a serious proposition, it is necessary that the Six should be brought round to regard this in a favourable light; it is also necessary that the Community be prepared to do quite a good deal for Australian primary exports, much more than they would do in the absence of association. If these conditions arose, despite the real difficulties presented by such an association in regard to Australian industry, the matter would deserve thorough consideration.

(c) Relations with Asian countries.

Japan.

The proportion of Australia's trade with Japan in 1960/61 was as follows (1):

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<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Exports</td>
<td>17.7%</td>
</tr>
<tr>
<td>Imports</td>
<td>6.0%</td>
</tr>
</tbody>
</table>

Australia's share of Japanese external trade in 1960 (calculated from the United Nations Yearbook of International Trade Statistics) was as follows:

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<table>
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</thead>
<tbody>
<tr>
<td>Exports</td>
<td>3.5%</td>
</tr>
<tr>
<td>Imports</td>
<td>7.6%</td>
</tr>
</tbody>
</table>

Australian exports in 1960/61 to Japan were comprised of: Wool 66 per cent; Minerals and coal 13 per cent; Wheat, sugar and other vegetable foods 8½ per cent; Iron and steel and other metals and manufactures 8 per cent; Hides and skins 1½ per cent; Meat and other animal foods 1 per cent; other items 2 per cent.(1) Over 99 per cent of exports were of primary products, including metals.

Australian imports in 1960/61 from Japan were: Yarns, textiles and apparel, 40 per cent; Iron and steel 24 per cent; other metals, manufactures and machinery, 9 per cent;
Crockery, etc. 4½ per cent; Toys, etc. 4 per cent;
Chemicals and Plastics 4 per cent; Fish 3 per cent;
Optical, etc. instruments 3 per cent; Pulp and paper 2½ per cent; other items 6 per cent. About 72 per cent of imports were of manufactured goods, 24 per cent of iron and steel and 4 per cent of foodstuffs.

The primary effect of economic union would be apparently trade diversion and the economies cannot be described as currently similar but potentially dissimilar, though there is a considerable area of competitiveness.

Whereas the opportunities for trade diversion in favour of Japan in the Australian market appear to be large, the opportunities for Australia in the Japanese market to displace imports from other countries do not appear so great. There are, for example, limited possibilities for trade diversion in a product such as wool where Australia already supplies most of the market. Moreover Japan's trade relations with other countries oblige her to purchase some foodstuffs such as grains and sugar partly from other sources. If integration took place it may be that the beneficial effect on Japanese incomes would raise demand for products supplied by Australia. The fact that any rise in incomes would be small in view of the size of the Japanese population does not alter this conclusion as many of the items exported by Australia would be demanded as a result of modest income increases.

On the import side Japanese manufactures would not only replace manufactures from other sources such as Britain but would put out of business a number of Australian industries.
The Japanese worker in the factory puts out an intensity of labour over long working hours and small remuneration which enables most manufactured goods to be turned out much cheaper than in Australia. Initial economies and a large local population have enabled many Japanese industries to be established on a larger scale than in Australia, leading to further cost advantages.

There are clearly limitations on the application of the law of comparative costs in any consideration of economic union between Japan and Australia. If the law were allowed free play the sequence of events would probably be as follows:

(a) substitution of Japanese manufactures for Australian manufactures;

(b) unemployment in Australian industries; and then either

(c) if Japanese goods were sufficiently cheap and of sufficient range to replace most necessary imports from other countries it is conceivable that Australian earnings in Japan and elsewhere from export of wool, etc., would be sufficient to pay for needed imports; or

(d) the Australian balance of payments would deteriorate, necessitating the application of import restrictions - in such circumstances the application of such restrictions to Japanese imports would not be incompatible with economic integration - some incidental protection for Australian industry still surviving would arise.

Either under (c) or (d) there would be serious unemployment, deterioration of the Australian standard of living and
difficult problems of distribution of income. This brings out the point made in the Brigden report (15) concerning the advantages of the Australian tariff. No satisfactory state of equilibrium would be reached until the standard of living of the Japanese worker approached that of the Australian worker. Without freedom of labour movement such a union does not appear to have any chance of success. The political obstacles to integration appear to make this impracticable.

Before leaving this question it may be noted that arguments are sometimes put forward designed to show that Japanese labour is not cheap. (16) It is a fact that wages are supplemented by a variety of social benefits. Moreover the Japanese industrial system is peculiarly patriarchal; not only is there little or no opportunity for workers to move from grade to grade but there is little scope for change of employment or the employer to dismiss. Japanese top executives are generally middle-aged. The Japanese clerk is relatively unproductive – methods of calculation are archaic and script is hardly such as to facilitate quick work.

Despite assertions that Japanese labour is not cheap the standard of living is much lower than in Australia. Food and housing are inferior and also the capacity to buy the more expensive consumer durables such as automobiles. Nevertheless with the current limitation of population in Japan

(15) The Australian Tariff (1929) page 84
there may be considerable rises in living standards from year to year. But at present wage differences between Australia are not the logical result of differences of productivity and, in the absence of protection in Australia, unbalance of trade would result (17).

Despite the fact that at present it is not possible to conceive of economic union with Japan it is worth while considering whether mutual trade cannot be greatly expanded to the benefit of both parties. Australian exports already exceed considerably imports from Japan and as it is not possible to consider it worth while for Japan to greatly increase her purchases under such conditions the first prerequisite appears that Japan should considerably expand her exports to Australia. With the removal of British preferences this may indeed be possible. There are also certain duty devices in Australia which tend to reduce Japanese trade but as these have been devised to protect Australian industry their reduction or removal implies some sacrifice by Australian industry. This, however, cannot be contemplated unless Australia develops a much larger industrial export than at present and Japan appears to be one of the markets which would be expected to receive some of these exports. It is not possible to work out under just what conditions an increased exchange of industrial goods with Japan would be possible. This might, for example, involve creation of mutual preferences, not an easy thing to arrange whilst the G.A.T.T. and United States policy remain as (17) See J.F. Deniau. The Common Market (1960) page 38.
influential as at present. (17A) This could envisage a structure where Australia concentrated on certain types of goods, perhaps capital intensive, whilst the Japanese took the market in certain types of goods where their production appears very efficient. These possibilities must not be ruled out in the new circumstances that may be created by the loss by Australia of its European export markets.

(17a) There may be other arguments against an exchange of preferences with Japan. At present Japan suffers preferences against her in the Australian market and the mere removal of discrimination might greatly increase Japanese exports to Australia. In such a case Japan would have little incentive to offer Australia preferential entry which could only be done at considerable cost to herself. On the other hand a reciprocal abandonment of protection on certain industries on a preferential basis might be more feasible.
influential as at present. In any case it appears to envisage a structure where Australia concentrated on certain types of goods, perhaps capital intensive, whilst the Japanese took the market in certain types of goods where their production appears very efficient. None of these possibilities must be ruled out in the new circumstances that may be created by the loss by Australia of its European export markets.

South and South East Asian countries

The proportion of Australia's trade with Burma, Ceylon, British Borneo, India, Indonesia, Malaya, Pakistan, Philippines, Singapore and Thailand in 1960/61 was as follows (1):-

Exports 6.8%
Imports 9.0%

The proportion of the external trade of these countries (including of British Borneo only Sarawak) in 1959 with Australia was as follows (18):-

Exports 3.0%
Imports 2.3%

Australian imports from this area (including all British Borneo) in 1960/61 were: Petroleum 14 per cent; Bags and Sacks 13 per cent; Rubber 10 per cent; Textiles 10 per cent; Timber 7 per cent and other important goods were cotton, jute, flax, hemp, kapok, nuts, tin and vegetable oils. Exports were rather diverse, about 36 per cent of vegetable foods (wheat, flour, sugar, malt, fruits); about 23 per cent were of animal foods (dried milk, infants' foods, butter, meats), about 18 per cent of metals and metal manufactures, wool 7 per cent.

(18) Calculated from United Nations Yearbook of International Trade Statistics. 
6 per cent petroleum products, animal fats (tallow, etc.)
3 per cent, chemicals 2 per cent and other items (including
live animals) 5 per cent.

Apart from petroleum, the scope for increased imports of
primary products into Australia from the region does not appear
promising. Timber is largely of hardwood variety and as both
Australia and Papua and New Guinea are rather well endowed
with hardwoods, free trade in timber would not be welcome.
Australia does in fact export sleepers to some countries of
the region and this trade could be increased. Other products
such as coconut from Ceylon and coffee from Indonesia might
have in fact to give way to increasing production in Papua
and New Guinea. However, the coconut export industry in that
territory has not recovered after suffering damage through
export of diseased material to Australia some years ago. In
the case of coffee the type of bean produced in the territory
is not very competitive with Indonesia and that country might
increase its trade at the expense of other suppliers.

In the secondary industry sector free entry of textiles
would severely hit Australian industry. If the problems were
confined to that industry they might be manageable but
increasing industrial production in some Asian countries
is widening the field in which severe price competition would
be felt. Moreover, the types of goods produced in these
developing economies tends to be similar to those produced in
Australia. Pakistan is an exporter of sporting goods at low
prices. In the G.A.T.T. a number of less-developed countries
such as India have expressed the wish for tariff reductions on such items as bicycles, small diesel engines, sewing machines, simple types of electric fans. A study of the Australian tariff indicates that it is the smaller and less elaborate types of industrial goods that are mainly produced in Australia; the tariff on the larger and more elaborate types is often at minimum level.

For the same reasons Australia would have little to hope for in the way of increased exports of industrial goods to many of these countries. Moreover, insofar as they do import such goods, they feel it necessary to buy in the cheapest market and would not, it it thought, like to give preferences to Australian products. This is not to say that it would be impossible to arrive at some mutually beneficial arrangement for exchange of industrial goods. As was suggested in the case of Japan, it would seem appropriate that Australia concentrate on goods of a capital-intensive type whilst the partners would send Australia labour-intensive manufactures. Such an agreement would fall short of a customs union and consequently, as noted above, difficulties would arise in implementation from the point of view of international trade policy rules.

Some measure of integration between Australia and Asia would, at present, seem most practicable in relation to countries such as Malaya, Singapore, British Borneo, the Philippines and Thailand. These areas have a more limited industrial output that say India and are also in less severe financial difficulties, so that a better prospect is
presented of a quid pro quo. Some of these countries have, moreover tended to combine together in an Association of South East Asian states. This body has so far not initiated a process of integration but this might well develop in due course. British Borneo and Singapore will be associated with this effort through political integration with Malaya.

Apart from this body there has been little desire for economic integration in Asia. This is probably through a fear of the smaller countries of being retarded industrially through association with larger countries such as India and Japan. It may also have been realised that integration is not without its costs as dearer goods may have to be imported than those obtainable from other areas. (19)

To select the eastern countries of this group for special consideration is not to suggest that Australian trade with the larger countries in the group can be neglected. To increase this trade presents considerable difficulties. Although the countries of this area have favourable trade balances with Australia they are tending to buy more of the goods of types supplied by Australia through bilateral barter deals with communist and near-eastern countries. Moreover, the population of these countries is very numerous and the standard of living very low and the economies precarious. As a consequence these countries look to Australia to give more than she receives; in the trade context, that is,

(19) Professor C.N. Vakil of Calcutta in "Economic Consequence of the Size of Nations" (1960) page 338 has suggested that the concept of integration runs counter to many of the political forces acting in these developing nations.
to import more than she exports to them though these countries are naturally anxious to accept commodities as a gift both from Australia, and much more importantly from larger countries such as the United States. It is therefore not possible to devise a formula for increasing exports to these countries. However, if Australia loses her markets in Europe she will no doubt look for a better balance in her trade with the area.

**Pacific Islands**

1.4 per cent of Australian exports in 1960/61 went to Pacific Islands associated with Britain, New Zealand and France but under 0.2 per cent of Australian imports came from that region. Whereas exports were very diverse and included, foodstuffs, coal and coke, petroleum products and a variety of manufactured goods, imports were mainly of minerals, phosphates and copra.

There are particular difficulties in the expansion of exports of produce of the Isles to Australia. Much of this produce is competitive with that of Papua and New Guinea; some, such as bananas, pineapples and sugar competes with produce of Australia. Phosphate deposits are becoming exhausted.

The opportunities for trade expansion in Australian produce to the Isles appears attractive but in the absence of a quid pro quo integration can exert no attraction for these territories. Particular difficulties arise in the case of New Caledonia of its association with the European
Economic Community; possibly some of the British territories may also be associated in the future.

Trade with Asia generally

Examination of the possibility of economic integration with various part of Asia have resulted in rather cautious and pessimistic conclusions. This is not, however, to put forward the view that the future of Australian export trade does not largely lie in that direction. Rather obviously it does lie with Asia in the field of primary products; less obviously it also lies there in the case of manufactured goods where Australian industry needs a large market in order to take advantage to the full of scale economies. Just how to create and ensure this large market is one of the problems to which it is not possible currently to give an answer.

In the case of increased trade in both primary and secondary goods it is apparent, however, that Australia will need to give a larger quid pro quo by importing more goods from Asia and that rises in living standards in Asia are essential - as is indeed apparent for many reasons, political as well as economic.
In the first half of the nineteenth century, the economic weakness of small states in Europe became apparent and movements towards integration developed in Germany. These movements were, however, exploited for political aggrandisement and out of a number of small states developed the German Empire, dominated by Prussia, which annexed many of the smaller territories.

In the early part of the twentieth century, economic integration was not of much importance. Between the two wars there were a number of attempts to form loose unions but many of these attempts were frustrated by reason of the fact that they were considered contrary to the most-favoured-nation clause of bilateral treaties. Nevertheless, the existence of exceptions in these treaties for some areas such as the British Empire, united under a common sovereignty, allowed the considerable extension of preferential systems in these associations. Preferences were not, however, extended between European countries.

The General Agreement on Tariffs and Trade, brought into force in 1947 as a result of United States initiative, contained provisions facilitating economic integration but preventing any extension of preferential systems falling short of integration and in fact providing procedures designed to work towards the elimination of these systems. The effect of these provisions has been quite revolutionary and has not always tended to greater access on more equal terms to the
trade of the world as was postulated by the Atlantic Charter.

The first move, the creation of Benelux, was one that the members had previously attempted to bring about in diverse ways. The major post-war moves, however, towards integration in Europe were inspired or encouraged by the United States. The freeing of trade and payments was accomplished in the framework of the Organisation for European Economic Cooperation, a body set up at the instance of the United States to ensure that its massive economic aid in the form of the Marshall Plan, was well used.

Eastern Europe remained apart from these moves though some attempts were made to improve the framework of East-West trade by discussions in the United Nations Economic Commission for Europe. The U.S.S.R., however, promoted a high degree of integration both in trade and industrial development between itself and the eastern European countries dependent upon it, under the auspices of an economic committee known as COMECON.

The first major move of real integration came about through French initiative. The Schuman Plan produced the European Coal and Steel Community, which provided for free trade in iron and steel between France, Germany and Italy and the three Benelux countries. In this body control over planning and production was largely vested in a High Authority and it was dislike of this supra-national form of regulation that appears to have been one of the main factors inducing Britain to abstain from participation in the Community.
This supra-national authority was later, however, to bend to national interests exerted through the Council of Ministers.

The success of the Coal and Steel Community appears to have inspired the six members to go further and at the Messina Conference they determined to enter into a customs union embracing all goods except coal and steel and nuclear materials; the latter was made the subject of another special agreement on the lines of that for coal and steel. Without much delay the relevant treaties were drawn up establishing the European Economic Community and Euratom. These were signed in Rome early in 1957, ratified later the same year and came into force at the beginning of 1958.

The desire to maintain trade between European countries in manufactures led Britain to attempt to negotiate a free trade area with the E.E.C. which would permit the maintenance of British agricultural policy and trade with the Commonwealth on preferential terms. The Six, however, saw the project as being favourable to Britain but not to themselves and rejected it. A free trade area on these lines was, however, created between Britain, Austria, Portugal, Switzerland and the Scandinavian countries with the aim of supporting the economies of these countries and putting pressure on the Six to come to terms with them.

After some attempts at group negotiation, Britain entered into direct negotiations with the Six and in 1961 applied to negotiate on conditions for membership of the Community. Other members of E.F.T.A. also applied for full
membership or association. However, Greece was the first European country to conclude an association with E.E.C., establishing a customs union over a lengthy transitional period. Ireland has also applied for full membership and Turkey for association. The political position of Finland, which is associated with E.F.T.A. but not strictly a full member, has not allowed her to apply for association with E.E.C.

The terms of British membership have not yet been agreed but it appears that Britain will join the Community on terms that British colonial territories and those territories that have recently gained independence may become associated with the Community. Some of these new countries do not, however, wish to be associated though they want to obtain the same advantages in other ways. It appears that some special safeguards will apply to the trade of India, Pakistan and Ceylon and that some steps will be taken to assist New Zealand. Canada and Australia appear, however, likely to lose all the special advantages they have hitherto enjoyed in the British market.

If this is the case, Australian export trade to Britain will suffer not only by the loss of tariff preferences and assured access for wheat, meat and sugar and other advantages but also by the establishment of high external barriers that will ensure that European products will always be available in Britain on more favourable terms than Australian products. As the potentiality for self-sufficiency.
in agricultural products is large, trade in foodstuffs is liable to decline rapidly over the transitional period; the outlook for metals is similar. Australian export trade will also have to bear the brunt of preferential treatment in Britain for the associated countries and territories. There has been some suggestion of an alleviation of the position regarding foodstuffs by means of comprehensive commodity agreements but it is neither certain that these will come to fruition nor what their terms would be.

Examination of the economics of the creation of customs unions indicates that two main factors are responsible for consequent economic changes — trade diversion and trade creation. Trade diversion arises from the cessation of imports from outside the union in favour of trade between partners of the union and it is occasioned by the preferential treatment accorded to imports from the latter. Trade creation is caused by increase of competition within the union and economies of scale resulting from specialisation. The effect of trade diversion on the welfare of outside countries is negative; whilst the effect of trade creation on outside countries is mixed in character it is unlikely to be strongly positive so that the overall direct effect on outside countries is likely to be negative. On the other hand the effect of trade creation on the welfare of the countries in the union is likely to be strongly positive and to outweigh any adverse effect of trade diversion. If this is indeed the case there will be economic growth in the union and this will
tend to increase trade with outside countries outweighing the effects suffered by these countries directly. If, however, the negative effects are predominant, as can well be the case, economic integration is generally disadvantageous.

Examination of the European Economic Community in the light of the above concepts and of related considerations formulated by economic writers indicates that the general effect of the creation of the union is likely to be favourable to welfare and to promote economic growth. This is at least the case in the field of manufactured goods. Evidence available to date does not enable this tentative conclusion to be verified by actual performance but the continued tendency of growth rates in the Six to exceed those in Britain is impressive. In connection with industrial integration many economic writers regard the increase of competition as being more likely to increase welfare than economies of scale and specialisation which they regard as over-rated. However, it may not be the case that these writers are fully seized of the importance of technological changes.

In the agricultural sector the Community appears to be primarily trade-diverting as relatively high-cost production of grains and other products will be stimulated and used to supply needs which could be more economically supplied from imports. It is as yet not clear whether integration will increase the efficiency of agriculture or whether relatively inefficient high-cost production will
remain. Even if efficiency is generally increased the costs of many products are still likely to be above those in the primary producing countries of the southern hemisphere.

It is difficult to appraise the considerations which have led Britain to seek to enter the Community with such urgency. These may lie mainly in the political field and include defence considerations. In the economic sphere it has been suggested that entry into the Community will give the British economy stimulus which it would be politically impracticable to impart in any other way. If the Community is indeed trade-creating in the industrial sphere there should be opportunities for Britain to increase its exports to the Community over the tariff barrier and in fact this appears to have been accepted by the United States in regard to its own trade. Outside the Community Britain could join with the United States in bargaining tariff reductions with the Six. Britain's own market, its protected markets in the Commonwealth and its other export markets ought, it might be thought, to enable Britain to secure any economies of scale possible in the Six.

In the agricultural sector British membership will lead to abandonment of the present policy of low food prices and high consumption in favour of the continental system. Whereas the abandonment of free entry for Commonwealth produce will enable the British budget to be relieved of the burden of subsidies to domestic farmers, the British economy will be burdened by the obligation to import relatively
high-priced continentally produced foodstuffs in lieu of relatively low-priced produce from outside countries; it is also likely to have to pay away some of the import levies it collects to subsidise the export of continental food surpluses to other areas. The rise in the cost of living is therefore likely to exceed any tax alleviations. Industrial costs will therefore bear some burden from the changes in the agricultural system and Britain's competitiveness in outside markets may suffer.

The effects of European integration on Australian exports vary according to the combinations under consideration. The European Free Trade Association is expected to have little effect because the association does not provide for free trade in agricultural products. On the other hand, the formation of the European Economic Community may lead to a loss of trade with the Six of considerable size, mainly in cereals. Membership of Britain in the Community will jeopardise a much larger volume of trade as, largely owing to tariff preferences and other agreements, Australia has developed a large trade in Britain in a variety of foodstuffs and raw materials including processed goods. It has already been noted in this chapter that British membership will mean that free entry of Australian goods into Britain will disappear and that preferences and commodity contracts will also most certainly go. Much of the British market will be supplied from the Community and associated countries and Australia will be left to compete against all comers.
for what remains of the British market. On many commodities suppliers from the American continent are more favourably placed than Australia to fill the remaining demand. The outlook for wool does remain reasonably favourable. Even if the enlarged Community achieves all that is hoped for the effect on Australian export trade in the foreseeable future is likely to be unfavourable.

On the import side European integration should not lead to price increases in the Australian market. The abolition of British preferences should in fact lead to more competitive buying by importers and some saving of foreign exchange.

The heavy loss of income from trade with Europe which may result from the extension of integration would render precarious the Australian balance of payments and would discourage overseas investment in Australia. The latter would also be adversely affected by the growth in attractiveness of the Community and associated countries as a field of investment. Australia may therefore find herself short of foreign exchange with which to pay for imports and this in turn could retard development. The Australian standard of living would fall and migration would follow suit.

In order to counter these adverse effects some revision of Australian policies would be necessary. Consideration could well be given as to the advantages and practicability of promoting schemes of integration between
Australia and countries with whom close relations are maintained. Australian association with the Community offers some attractions but it is unlikely that the Six would consider anything short of a customs union nor would a preferential association on the lines of those afforded the African countries appear acceptable internationally.

Association of Australia with the Community would render the disposal of Australian primary production a Community problem. This would no doubt be a favourable development for Australia but would be an unwelcome responsibility for the Six. On the industrial side the enlarged Community would be assured of a large share of the Australian market. Free entry for European goods would mean a thorough overhaul of Australian industry no doubt leading to specialisation. Just how Australian industry would be developed on competitive lines to supply both the Community and outside countries with certain goods is not clear though such a development should not be impossible.

Australian migration should be assisted by closer links with Europe. The whole concept is, however, very far reaching and has not to date evoked much enthusiasm either in Europe or in Australia.

Australian association with other members of the Commonwealth possesses little to commend itself except in the case of New Zealand which is an important market for the products of Australian industry. The problems of the development of New Zealand industry should be manageable.
However, such a union would still be a relatively high cost economic island dependent on the vagaries of the market elsewhere for primary products in order to pay for necessary imports. Integration with New Zealand, although desirable, still leaves Australia with the fundamental problems posed by less of European markets.

Japanese association with Australia in two-way free trade is conceivable without unduly impoverishing Australia if the price of Australia's traditional exports such as wool becomes sufficiently low. However if Australia's exports were confined to primary products, Australian industries would be put out of production and it would be difficult to develop and diversify the Australian economy and maintain employment. Such an association only seems economically feasible if the Japanese standard of living approaches that of Australia and if there were free movement of labour.

The association of South East Asian countries with Australia would not confront Australia with such vigorous industrial competition and might be practicable, especially if these countries decide to integrate amongst themselves. It is difficult to conceive of an association, however, with the South Asian states as these states are very populous and very poor and those that have developing industries are entering the same fields of production as Australia. These countries are unlikely to afford Australia a quid pro quo for association and therefore this would not be a solution to Australia's economic problems consequent
on loss of its European trade. That is not to say that
trade with the area is not important to Australia and steps
may need to be taken to get this into better balance.

It will have been noted that the practicability of
Australia participating in economic integration schemes
is thought of mainly in terms of complementary rather
than competitiveness. This is because developing countries,
unlike fully industrialised countries, cannot afford to
submit their modicum of industry to unrestrained competition.
Although the possibility of association with Europe on these
terms has been seriously considered it is subject to the
proviso that ways must be found to build up a range of
large-scale competitive industries in Australia. Even the
industrialised countries of Europe are hesitant to expose
their industry to competition from low-wage countries and
this is also relevant to Australia. What might be practicable
and of mutual advantage is some preferential arrangement
between Australia and industrialised Asian countries,
notably Japan, but it is difficult in the current
international climate to see such an arrangement being
sanctioned by other countries. In any case it would be
necessary for Australia considerably to increase its imports
from Japan before that country would give Australia preferences
on industrial goods.

Whether or not any association or preferential
arrangement is feasible it is clear that Australia must
look increasingly to Asia as a market for both primary
products and manufactures. So far as the latter are concerned there may be scope for a two-way specialisation whereunder Australia exports capital-intensive goods to Asia and imports from Asia labour-intensive goods.

Other regions such as Africa and Latin America may also offer scope for export of Australian goods though the competitive nature of some Latin American countries in wool, cereals, meat and dairy products and fruit with Australia limits the field.

The possibility of some contraction of total exports of foodstuffs consequent on the disappearance of the European market has to be faced although every effort will need to be made to make up these losses by export to other areas. If the proposed world-wide commodity agreements ever come to fruition it may be possible for increasing quantities of primary products to be moved to less-developed countries.

The effects on the Australian economy of the changes in trade patterns are likely to be such that it may become, irrespective of the existence of special associations, necessary to build up large-scale specialised industries and to expose weaker industries to increased competition from imports as only in this way can costs in Australia be made competitive with those in other areas. In such case means must be found both to ensure continued inflow of capital for development and to ensure export markets of
adequate size. This development is not, however, inevitable and will require a good deal of conscious effort. An easier but unsatisfactory alternative would be to drift into an even more highly diversified and high-cost economy than at present under the protection of import restrictions imposed for balance of payments reasons. This prospect promises little for the Australian standard of living or for development.
In the light of the comments made in the foregoing chapters it will be useful to conduct some further examination of the theory of economic integration. At the same time use will be made of re-statements of the theory in works not hitherto considered, particularly the short summary in Professor Meier's book (1) and the extensive treatment of the subject by Professor Balassa, (2) who has not only brought the authorities together in a more complete and adequate way than was independently attempted in the foregoing pages, but has also undertaken an exhaustive exposition of the dynamic factors significant in economic integration. The theory will be reviewed under headings following largely the method adopted by Professor Meier.

**Competition.**

Economic integration has the feature of combining freer trade and more protection and for this reason a particular scheme may be favoured by free-traders and protectionists alike. (3) Most writers agree that, so far as developed countries are concerned, increase of competition is the outstanding virtue of economic integration. This can be equated with "trade creation", using this latter term in a narrow sense rather than in the broad sense employed in Dr. Corden's table (4) which brings out that the direct effects of trade creation are beneficial to the members of a union rather than to outside countries. In the narrow sense the replacement of high-cost domestic production by low-cost production.

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from another member of the integrated area, therefore promoting an economic shift of resources into more efficient production within the region. (5) It is more likely to result the more the members are initially similar in the products they produce but different in the pattern of relative prices at which they produce them. (6) Professor Meier adds that initial tariff rates should have been high.

The vice of economic integration, on the other hand, is "trade diversion". Where trade between members and non-members is replaced by trade within the union the international division of labour will be worsened to the extent that the outside source of supply is actually a low-cost source and output is diverted from the low-cost source to the high-cost source within the union.

Professor Meier states that trade diversion is less likely to occur the less competitive are the products of members with outside imports. (6) The term "competitive" in this context appears to mean that the products of the member states are the same/or substitutes for products imported from outside countries. It does not mean competitive in the price sense, for if the products of member states were costly than those of outside countries there would be no loss of welfare in the substitution of products of members for those of other countries.

This interpretation of the word "competitive" is consistent with Professor Meier's further proposition that trade diversion will be the less the lower is the "average" tariff level on outside imports as compared with the level of the tariffs before union. (6)

Although this further proposition conveys a useful general picture that prices to the consumer should not be higher after integration than before, it rests on the assumption that tariffs are always fully effective and consequently are the main determinant of prices. While tariffs may at some stage have in fact corresponded to protective needs they are often out-of-date and competition within a country may have ensured that some of the benefits of improvements in productivity have been passed on to the consumer.

There is, moreover, a relevant case where an average tariff level has not been changed but it can be reasonably assumed that, at least in the short run, integration will have increased welfare. This is a case, exemplified by the E.E.C., where a common tariff has been fixed "across-the-board" at the average of existing tariffs. The fact that the resulting common tariff is not fully effective appears to be borne out by the readiness of the E.E.C. to cut industrial tariffs by a percentage across-the-board and that it does not feel necessary when offering to do so to provide for extensive compensatory measures to assist industry as is the case in the United States Trade Expansion Act, which also provides for similar tariff cuts.

The rationale of the above statement is illustrated in the following example. Country A has a tariff on a product of 1 per cent, country B's tariff on this product is 5 per cent and C's tariff 9 per cent; the common tariff of the union is 5 per cent. It appears reasonable to assume that A, in the case of a developed country, can expand production without increasing costs. Moreover transport costs could reasonably be assumed not to be greater between A and the other
members than between the latter countries and outside suppliers. In such a case a common tariff of 1 per cent would have been adequate to assure for A the market of B and C against outside suppliers. In the context of considering the benefits or otherwise of changes in production from outside countries to A it does not seem justified to assume tacitly that oligoplistic forces in A will take advantage of the excess protection afforded to the industry by the tariff. It seems reasonable, therefore, to assume that consumers of the product in the union will be able to purchase it at a price around 1 per cent above that at which it could be imported from outside countries. In the long run it is undeniably desirable that the excess protection be removed. Any proposition regarding the average level of tariffs before and after union should therefore preferably be qualified by stating that it is assumed that in all cases the tariffs are fully effective and it would with advantage be pointed out that it is important that a common tariff be fixed no higher than necessary to protect the most efficient branch of the industry in the union.

Lipsey has reformulated an earlier proposition regarding economic self-sufficiency in relation to trade diversion by stating that "given a country's volume of international trade, a customs union is on balance more likely to raise welfare the higher is the proportion of trade with the country's union partner and the lower the proportion with the outside world." Furthermore, the "union is more likely to raise welfare the lower is the total volume of foreign trade, the lower is foreign trade, the lower must be purchases from the outside world relative to purchases of domestic commodities." (7) However, it is

possible that pre-union trade between the partners was small because the partners produced the same kind of products and each protected itself from imports against the others, whilst trade from the outside world may have been large because the outside countries supplied complementary goods. This is in fact the way trade of European countries had developed over the period 1914–1939. In such a case union could be expected to be beneficial.

From LIPSEY's proposition Professor MEIER has deduced that economic integration is less likely to benefit poor countries than a group of "sizeable countries which practice substantial protection of substantially similar industries." (8) However, it will be seen later that the chief value of economic integration to developing countries does not lie in competition.

Professor MEIER also points out during the course of his discussion of these issues that whether trade creation or trade diversion is likely to be dominant depends on the elasticities of demand for the imports on which duties are to be reduced and the elasticities of supply of exports from the members and outside sources. This is a subject developed at some length by Professor MEADE (9) and commented upon below. Professor MEIER does not repeat the proposition of Meade that the benefits likely to obtain are greater in the earlier stages of tariff reduction than in the later. This proposition has been subjected to considerable examination at pages 105–110 (supra), where it was noted that special circumstances arise at different stages in the reduction of tariffs which

necessitate the examination of supply elasticities at these stages and that these special considerations qualify the general acceptability of Meade's proposition. Some misgivings have also been experienced regarding Meade's proposition that economic gain is the more likely the larger the proportion of world trade, production and consumption covered by the union (10) and it is to be noted that this proposition is not repeated by Meier. It must be stressed that the objection to large unions is not solely related to their influence on their terms of trade with the outside world but also to the fact that they follow extremely "trade diverting" policies in individual sectors which may have the effect of depriving other countries of export markets which cannot be replaced. (11)

Professor Meade has traced at some length the effect of elasticities of supply and demand on the extent of trade diversion and trade creation caused both directly and on account of secondary ensuing changes. (12) The secondary effects include those resulting from the substitutability of the products concerned with other products and from complementarity. If the union is not one involving important countries, the elasticity of demand of the outside world for products of the union and the elasticity of supply in the outside world of products required by the union are unlikely to be altered by the formation of the union. However, it may be noted that within the union elasticity of demand for products of the union involves "consumption effects"; if the price falls in one country due to imports from a more competitive partner, there will be increased consumption and also an increase in welfare, on the

reasonable assumption that the lost customs revenue can be raised in a manner having less effect on welfare than a customs duty. (13) Professor Johnson has, however, pointed out that diversion of consumer expenditure to the tax-free good from products which are taxed will increase the amount of revenue to be raised by other methods and that there will be a net gain only if the reduction of consumer expenditure (14) is less than the gain in consumer's surplus on the tax-free commodity. (15)

Professor Meade has also stated that where the original barriers between the partners in a union are all quantitative, their removal is unlikely to have adverse effects. This appears to be unexceptionable where these barriers were protective in design and where their removal does not reduce any quota available to outside suppliers. It follows because, on the assumption that the outside countries are the cheapest suppliers, (and that there is no tariff barriers), those suppliers will still be able to send their quota into the importing member whilst the competition that that member has to experience from its partner in the union cannot but be beneficial. If, however, the restrictions are imposed for balance-of-payments reasons, the removal of restrictions between partners can be detrimental.

Suppose, for example. A and B enter a customs union and that

(13) J.E. Meade, op.cit., pages 37/41. (14) The reduction in consumer expenditure is the amount of tax formerly levied on the product no longer purchased, which tax will now be levied directly on individuals. The indirect tax represents a measure of the value to the consumer of the product in question over and above its cost of production. (15) H.G. Johnson, op.cit., page 18.
countries a product in inelastic supply, say caviar. Removal of restrictions will cause A to import caviar which formerly it did not do and the earnings from caviar exported to third countries, unless the demand is very inelastic, will be reduced. Suppose also that A is formerly severely restricting the import of motor cars from all sources and that restrictions are removed on motor cars imported from B. If motor cars are in elastic supply from B, A might as well import freely from all sources (in order to avoid excess costs) as, whether or not it does so, consumers in A will import all the cars they need. This may constitute an undue drain on the payments position of A. On the other hand, if cars are in inelastic supply from B, A may be able to preserve itself from over-importing cars by cutting off imports from other sources. This may constitute a strain on its trade relations with third countries and may also mean that it is paying more from B for cars than it would have to do from other sources, even when the tariff preference is taken into account.

It is doubtful, therefore, whether import restrictions imposed for balance of payments reasons ought to be generally removed between partners in a union. If both partners are in balance of payments difficulties and of roughly equal industrial strength, they may indeed be able to obtain some compensating advantages through removal of mutual restrictions. The selective liberalisation plan of O.E.E.C., which was, however, accomplished without removal of tariffs, may have proved workable for these reasons. In the E.E.C., moreover, removal of restrictions is made more feasible by mutual economic support.

Although Professor Meade did not insert any qualifications into
his analysis regarding removal of import restrictions, it may be noted that, in discussing the "tertiary" effects resulting from changes in the balance of payments position caused by union, he points out that the net results on welfare (in and outside the union) will depend on elasticities of supply and demand for imports and exports. (16)

A further important aspect of competition within a union is the benefit that may result from "forced efficiency" - the fact that producers are obliged to adopt the most efficient methods of production. (17) It is hardly necessary to add that this is the more likely to occur the less protective are barriers to outside imports. The latter aspect is also important in order to guard against the fruits of competition being lost by monopoly and restrictive trade practices.

**Agriculture.**

Professor Johnson has pointed out that integration of a predominantly agricultural country with an industrial country may be disadvantageous for the former because it may be exploited by the manufacturing country, which may be relatively inefficient, so that the agricultural country loses any comparative advantages it has without compensation. (18) He does not appear to attach great importance to the brake on manufacturing development in the agricultural country though in practice it seems that there are a number of reasons, including those related to employment, why any retardation of manufacturing development is important.

Little attention appears to have been paid by economists

to the theory behind "managed" integration of the agricultural sector of industrial countries such as those of the E.E.C., where are to be uniform prices/set for producers within the union and complete protection is given against imports from outside countries. From the point of view of the outside supplier this appears very diversionary.

From past experience it can be assumed that resources employed in agriculture will not in fact be diverted from that sector merely because of its inefficiency by world standards. Economic integration therefore offers some prospects of better utilisation of resources within the union, if prices are not set too high, by ensuring some controlled degree of competition and by setting a climate where innovations are effected in that sector. Increase of agricultural productivity may be conducive to better national growth rates and this will spill over into beneficial effects for the outside world at large (19), though these benefits may not accrue to outside agricultural countries. If, however, prices are set at levels affording an increase in overall protection welfare both within and outside the union will suffer. If surpluses result and are given away to needy countries, there is room for argument that agricultural protectionism is not without its benefits but it is not easy to assess these against the losses in welfare already noted. So far as the needy countries are concerned their benefits can be ascribed to political situations whereby the wealthy countries are willing to forego welfare which otherwise they would not be agreeable to do.

(19) See Dr. Corden's table, page 74, supra.
Specialisation and Scale.

Economic advantages resulting from integration can occur through specialisation, that is the reduction of the number of processes performed in one plant, which becomes possible with expansion of the market. Advantages may also occur from economies of scale. These can either be internal economies, resulting from expansion of the size of the plant, or external economies, induced by an expansion of the number of plants in a given industry or by the simultaneous development of a number of industries. External economies may bring with them agglomeration, or the centering of industries in particular regions, which leads to unbalanced development of the union, whilst internal economies may lead to a growth of monopoly.

Whether and to what extent industrial countries are likely to benefit through integration from specialisation and economies of scale is controversial, as will have been noted from the discussion on pages 76-80 (supra). Professor H.G. Johnson considers likely gains resulting from European integration through specialisation to be insignificant. (20) Carter and Williams consider that in certain industries the British market has not been big enough to encourage the growth of specialist producers of equipment who themselves might have created new possibilities of progress. (21) Professor Balassa has concluded that European integration will indeed permit the exploitation of economies internal to the firm that had not previously been forthcoming because of the limited size.

of the market. (22) In order to maintain this hypothesis he has, however, had to take considerable pains to detect faults in empirical studies that have indicated opposite conclusions. If indeed it be accepted that there are advantages to be derived from economies of scale and specialisation through integration of industrial countries, this may in fact only apply to a limited number of industries when countries the size of Britain are in question. If so, selective tariff reductions to negligible levels on these products would seem to be a simpler solution than integration. Insofar as developing countries such as Australia are concerned it is generally accepted that industries such as the manufacture of certain chemicals suffer from serious cost disabilities on account of their small size.

Professor Meier makes the point that, if the supply of productive factors is limited, the scale of the national economy will not be increased unless union results in a substantial increase in factor mobility. However, normally it is considered that factor shortages would be remediable and that large-scale industries would not be established were this not the case.

As in the case of competition, the advantages of economies of scale will accrue to the integrated area rather than to outside countries. There is, however, at least one set of circumstances in which outside countries may benefit. If the integrated area becomes competitive with another large outside supplier, because increase in scale of production, third countries importing the goods in question should benefit through lower prices.

(22) Bela Balassa, op.cit., page 118.
Terms of Trade.

Professor Meier points out that the possible improvement in the terms of trade resulting from integration rests on the presumption that the demand by members of the union for imports from outside countries will be reduced or that the bargaining power of the members will be increased. This will depend, he states, on whether or not the members of the union have sufficient monopolistic or monopsonistic power to influence their terms of trade. (24) Put in another way, a union is more likely to gain from improved terms of trade the less elastic is the foreign supply of its imports and the less elastic the foreign demand for its exports. (25) That a powerful union is able to exert considerable bargaining power is evidenced by the way the E.E.C. has influenced the conditions set by the United States for the Kennedy round of tariff negotiations.

Economic integration and developing countries.

Professor Balassa has advanced two propositions regarding the size of a union - the larger the size of the union, the greater the potential gains from integration for the world as a whole (26) - the greater the increase in the market of the participating economies, the more will the world and member countries benefit. (27) The size of a union of less-developed countries, measured in terms of G.N.P., is likely to be small, so that on this criterion little benefit can be expected. However, the association of a number of small countries is likely to bring about a greater improvement in

(24) Gerald M. Meier, op. cit., page 149. (25) H.G. Johnson, The Economic Theory of Customs Unions, op. cit., page 22. (26) However, the dangers of trade diversion in this case have been noted. (27) Bela Balassa, op. cit., page 38.
world efficiency than the integration of two large economies and the
gain for individual member countries will be positively correlated
with the increase in market size. (28) The relative advantage to
these countries is increased if dynamic factors, such as the
possibilities of future development, are taken into account.
Professor Meier stresses that the prospect of dynamic gains from
new investment is likely to be more significant than gains from
reallocation of existing production. (29)

Propinquity is an important element if advantages are to be
reaped from economic union. For this reason integration of a
restricted area may be more successful than too far-flung a union.
This is particularly so where transportation facilities are
poor as is likely to be the case between many less-developed
countries.

In these countries considerable benefits may be obtained
from the fuller use of capacity formerly under-employed because
of the small size of the market and in other cases suboptimal size
plants may have been established through the same cause. Despite
transport disadvantages the integration of developing economies
offers more possibility of gain from internal economies than does
that of large industrial economies. (30) A study of New Zealand (31)
industry revealed a high proportion of industries where increasing
productivity obtained with growth in size. (32) In Latin America

Zealand, although not an under-developed country, because of its
high living standards, can nevertheless be considered as a "develop-
ing" country because it is immature industrially. (32) J.W.Rowe,
"Productivity and Size in New Zealand Manufacturing Industry",
there are indications that plants in many industries are operating below optimal size. (33) Except on the west coast the large undeveloped equatorial area sets some limit on the intercourse between countries in the south of the region and those in the north and integration may be expected to be limited for the moment to groups on either side of the equator.

Professor Balassa has also pointed out that economic integration may also be of considerable significance to developing countries in that it will facilitate simultaneous development of a number of industries. This gives rise to external economies through the transmission of innovations and technical change. (33) However, there is clearly some measure of conflict, where resources are limited, between the concepts of multiple development of industries (34) and scale. A concept that combines something of both ideas is specialisation between operations so that one plant does not produce the complete product. This may be of significance to developing countries where transportation facilities permit.

Developing countries may also benefit from union through the attraction of foreign capital, both portfolio and in the form of direct establishment of plants, anxious to get behind the tariff wall; governments are also more able to attract foreign loans through their increased stature. Outside countries are unlikely to suffer through increased industrialisation in developing countries, even though this appears prima facie to be trade-diverting, because of growth potentialities and the high propensity to import.

(33) Bela Balassa, op. cit., page 139. (34) Professor Meier considers that uneconomic multiplication of new industries may be guarded against in a union by the joint administering body.
There is some danger that planning of an economic association of developing countries will fail to give adequate weight to the benefits of competition and that monopoly influences will, as a result, impair the benefits which ought to be derived from the larger market. This is particularly the case with "complementarity agreements" and other schemes of limited integration such as are discussed in the following section.

It has already been noted that industry may tend to settle in regional pockets or agglomerations which will accentuate regional inequalities in income and development. Professor Meier considers that common institutional arrangements resulting from union may tend to promote a regional development programme and also to avoid wastes of watertight compartments of industrialisation. (35)

Preferences for development.

Some economic effects of sector integration have been discussed in Chapter 9. (36) Another form of limited arrangement possible between developing countries is where one member of a group specialises in the production of one product, for which it obtains free entry, on a preferential basis, to the markets of other members of the group. Such a scheme has all the disadvantages of sector integration in regard to the allocation of resources and, as noted above, may tend to monopoly positions through the discouragement of competition. Nevertheless, when allowances are made for the special needs of developing countries for industrialisation and (35) As well as the effect in note 34. (36) See pages 216/218, supra.
the concomitant needs for adequate markets for large-scale industries (37), particularly if the preferences are granted for only a limited number of years. The industries established, possibly with international aid, may well not exist at all in the countries concerned prior to integration. This tends to minimise waste of existing employed resources but negates any benefit through the classic concept of "trade creation" through increased competition.

Any such scheme between a group of countries would probably be a multiple one, as each member of the group could seek a quid pro quo through the establishment of new industries with wide markets. If geographical considerations permit, countries could agree to specialise in complementary products for joint use in a finished article such as a motor car. (39) Successful operation of such schemes may be jeopardised if some of the members get into serious balance of payments difficulties periodically, because in such circumstances they may attempt to cut down imports from other members, thus destroying the balance of the scheme.

The level of tariffs under such schemes would need to be high enough to assure the market to the preferential partner but not so high as to cause the importing country problems due to the high cost of the imports in question. A scheme is likely to be more stable if the products to be exchanged are essentials than if they are consumption-creating products that the importing country may wish to...
do without when in balance of payments difficulties. Preferential import licensing would further raise the preference assured by the tariff and has its own particular dangers. (40)

Schemes of this nature are at present contrary to G.A.T.T., although they are provided for in Article 15 of the Havana Charter, which never came into effect. Chile attempted in 1954/55 to secure recognition of these schemes by the G.A.T.T. but was not successful in the face of doubts by the leading countries whether such schemes would promote desirable economic development. (41) Preferential arrangements aiming to benefit less-developed countries are likely in the near future to be discussed both by the G.A.T.T. and the United Nations Conference on Trade and Development.

The Latin American Free Trade Association agreement contains provisions for negotiation on industrial products, hitherto not traded in the area, on a bilateral basis, and also for "complementarity agreements" between members. Both of these may result in biased forms of integration in certain sectors. Although the free trade agreement does in fact provide that "substantially all the trade" between members shall be free, as required by the G.A.T.T., in fact Latin American trade in industrial goods has been insignificant (42) so that most of the industrial sector may fall outside the multilateral free trade area created by the "common lists" of products to be established in the association. If these somewhat unorthodox

provisions regarding new industries were challenged in the G.A.T.T., the argument could be put forward that these provisions were an attempt to extend the free trade area beyond the minimum required by the G.A.T.T. and that this ought to be considered laudable.

Conclusions.

It is not possible in a few words to summarise the theory of economic integration. Even in its classical form, limited to the effects on welfare of trade creation and trade diversion in the narrow sense, it is only very laboriously explained by static analysis and may require a general equilibrium approach in order that the various inter-related changes in trade, prices and welfare can be adequately appraised.

When the theory approaches the field of specialisation and economies of scale, it becomes a subject of controversy in relation to industrial countries; in the case of developing countries it relies largely on the expected dynamic benefits to be gained from economic growth.
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